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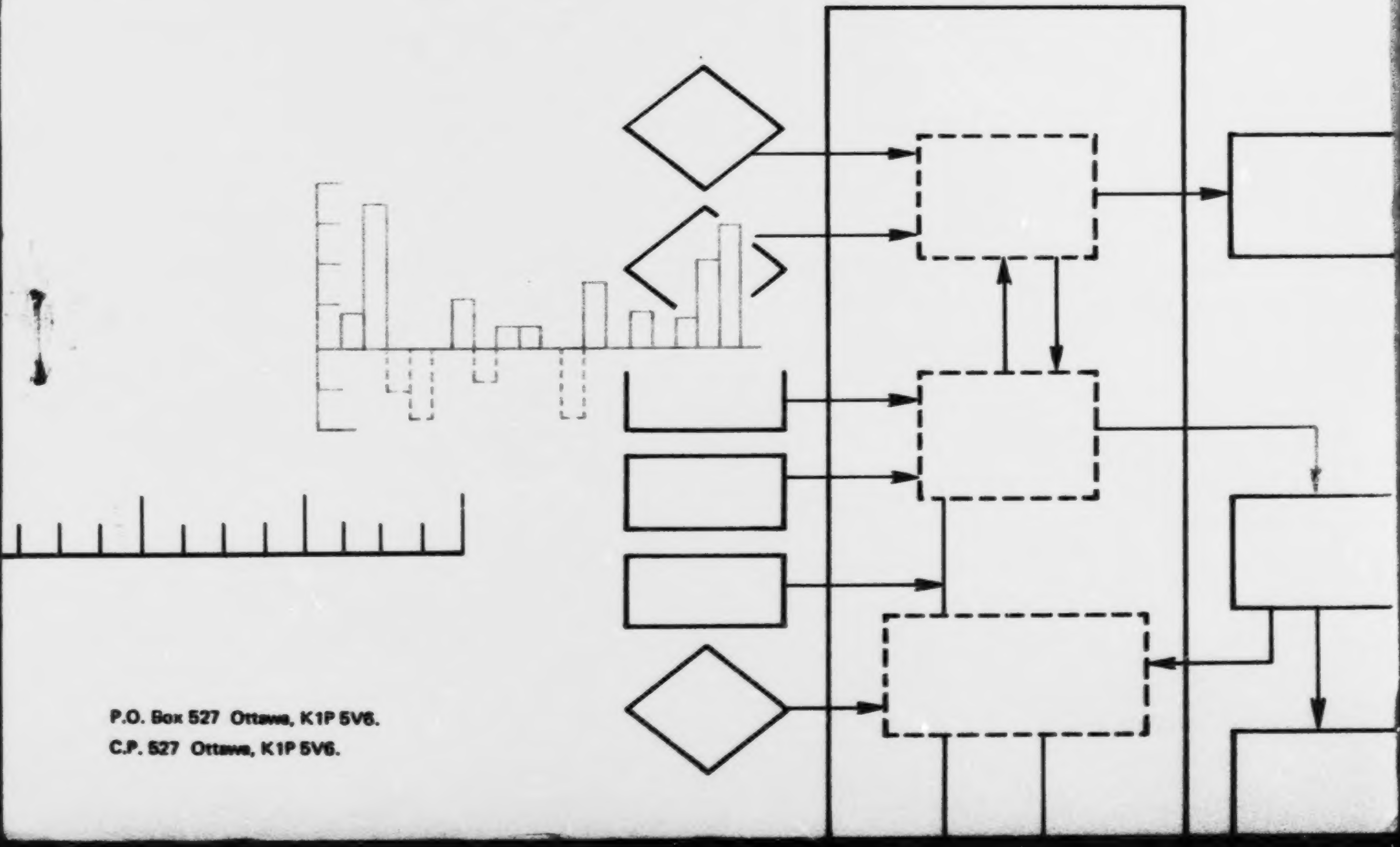

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DISCUSSION PAPER NO. 240

Governments and the Residential Mortgage Market II: Programs and Evaluation

by George Fallis

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RÉSUMÉ

Le présent document, ainsi qu'un autre de la même série intitulé Governments and the Residential Mortgage Market I: A Normative Analysis, traitent de l'intervention de l'État dans le marché des hypothèques résidentielles. Le document précédent met en place le cadre normatif propre à l'économie du bien être, l'applique aux marchés des hypothèques et du logement au Canada et présente des recommandations au sujet du rôle de l'État dans le marché hypothécaire résidentiel. Le présent document décrit la participation effective des gouvernements fédéral et provinciaux dans ce domaine et en fait l'évaluation en la comparant aux recommandations portant sur l'économie du bien-être.

L'analyse de l'économie du bien-être conclut à la nécessité de la présence de l'État sur le marché hypothécaire résidentiel, mais seulement dans certaines circonstances particulières limitées. Entre autres conclusions découlant d'une telle analyse, on recommande que l'assurance hypothécaire continue d'exister dans le secteur public, ou qu'elle cède la place à la réassurance des hypothèques privées. Des prêts hypothécaires publics devraient être disponibles pour les cas où des emprunteurs ne peuvent obtenir de crédits, soit parce que les prêteurs du secteur privé sont incapables de regrouper des prêts à risque élevé, soit qu'ils disposent d'une information incomplète. Mais avant d'accorder des prêts publics, il faudrait étudier soigneusement le cas de ces

emprunteurs ainsi que les raisons pour lesquelles ils sont incapables d'obtenir ce qu'ils souhaitent. Des prêts hypothécaires du secteur public pourraient aussi être consentis dans le cadre d'un programme d'aide à la rénovation des maisons, afin d'accroître la consommation dans le secteur du logement, ou encore être intégrés à une politique budgétaire et monétaire optimale destinée à stabiliser l'économie.

Depuis le début des années 70, la participation des gouvernements fédéral et provinciaux au marché hypothécaire a été intense. Les chapitres 2 et 3 présentent et décrivent les principaux programmes des deux paliers de gouvernement, et soulignent le but et les particularités des instruments d'intervention. Parmi ces programmes publics, actuels ou passés, mentionnons l'assurance hypothécaire, les prêts hypothécaires visant à stabiliser l'économie nationale et le secteur du logement, ainsi que d'autres prêts hypothécaires, soit à l'intention des emprunteurs qui ne peuvent en obtenir ailleurs, soit dans le but de financer la construction de logements publics, de logements locatifs, l'achat de maisons et la rénovation de logements.

Il est possible d'évaluer cette contribution du gouvernement fédéral et des provinces en comparant les programmes existants avec ceux dont l'économie du bien-être favorise la création. Cette évaluation est présentée au chapitre 4. Il est important de voir si les objectifs officiels de l'État sont semblables à ceux qui lui sont impartis par l'économie du bien-être. De façon générale, les deux ensembles d'objectifs sont effectivement identiques, bien que la terminologie employée d'habitude pour les décrire soit un peu différente. Toutefois, à un niveau plus détaillé, les objectifs officiels n'intègrent pas une perspective suffisamment cohérente et bien articulée du rôle de l'État dans les marchés hypothécaires pour servir de guide à une évaluation des programmes actuels ou à une comparaison avec le cadre normatif de l'économie du bien-être. Ainsi dans notre comparaison des programmes courants avec les programmes recommandés, l'évaluation est-elle implicitement fondée sur les données de l'économie du bien-être.

L'assurance hypothécaire et les programmes de prêts qui en découlent correspondent à peu près aux politiques préconisées, mais il n'en va pas généralement de même pour les activités de prêt dans le domaine du logement social. Le prêt hypothécaire n'est pas un bon moyen de résoudre le problème que pose l'insuffisance de la consommation dans le domaine du logement, non plus que celui de la redistribution des revenus. Selon les principes de l'écononomie du bien-être, la meilleure manière de procéder, dans le premier cas, est d'assurer des allocations de logement ou une aide à la rénovation (ce qui signifie que, pour ce genre de programme, les prêts hypothécaires devraient être maintenus), et la meilleure façon de redistribuer les revenus est de recourir aux transferts en espèces. L'État n'a pas tellement utilisé les programmes de prêts hypothécaires pour stabiliser l'économie, sauf très récemment, et il est difficile de voir en quoi ils diffèrent d'une politique optimale. Certains efforts ont été faits pour stabiliser les fluctuations dans le secteur du logement (à l'encontre des principes de l'économie du bien-être) avec, comme résultat général, une atténuation de certains creux du cycle, mais aussi de nouveaux sommets. Ces tentatives n'ont probablement pas entraîné une réduction du prix à long terme des logements.

ABSTRACT

The purpose of this and a companion discussion paper - Governments and the Residential Mortgage Market I: A Normative Analysis - is to examine government involvement in residential mortgage markets. The companion discussion paper sets out the normative framework of welfare economics, applies it to mortgage and housing markets in Canada and develops recommendations about what the role of government should be in residential mortgage markets. This discussion paper describes the actual role of the federal and provincial governments and evaluates it by comparing it to the recommendations of welfare economics.

The analysis of welfare economics concluded that a government presence in residential mortgage markets is called for but in certain specific limited circumstances. It recommended that public mortgage insurance should be continued or public re-insurance of private mortgage insurance instituted in its place. Public mortgage lending should be available as an instrument to use when there are unserviced borrowers because private lenders may be unable to pool high risk loans or are acting on incorrect information. But before such lending is done, there ought to be a careful study of the existence of unserviced borrowers and why they have not been granted loans. Public mortgage lending might also be used as part of a renovation assistance program designed to increase housing consumption or as part of an optimal fiscal and monetary policy to stabilize the economy.

The involvement of the federal government, and of the provincial governments since the early 1970's, in mortgage markets has been extensive. Chapters 2 and 3 provide overviews and describe the main programs of the federal and provincial governments, emphasizing the objective and details of the instruments of intervention. There are (or have been) programs providing public mortgage insurance, mortgage loans to stabilize the national economy and the housing sector, mortgage loans to unserviced borrowers, and mortgage loans to finance the construction of public housing, rental housing, the purchase of homes, and to finance the renovation of older housing.

This involvement of federal and provincial governments can be evaluated by comparing actual programs with those programs which were recommended by welfare economics. This is done in Chapter 4. It is important to establish whether the stated objectives of government and the objectives assigned to government by welfare economics are similar. In a broad sense the two sets of objectives prove similar, although the terminology usually used to describe each is somewhat different. However, at a more detailed level, existing stated objectives lack a sufficiently coherent and well-articulated view of the role of government in mortgage markets to guide an evaluation of existing programs or to compare with the framework of welfare economics. Thus the evaluation by comparing actual programs with recommended programs implicitly assumes the values of welfare economics.

The mortgage insurance and residual lending programs roughly correspond to the recommended policies but the bulk of the lending under social housing programs does not. Mortgage lending is a poor approach either to solving the problem of housing underconsumption or to meeting the need for income redistribution. Welfare economics suggests the best way to deal with the former is either with shelter allowances or renovation assistance (so mortgage lending under this type of program should be continued) and the best way to deal with the latter is with cash transfers. Public mortgage lending has not been extensively used to stabilize the economy except very recently and it is difficult to assess how it differs from an optimal policy. Some attempt has been made to stabilize housing fluctuations (which was not recommended by welfare economics) which on balance has made some troughs shallower but also some peaks higher. These attempts are unlikely to have resulted in any reduction in the long run price of housing.

1 INTRODUCTION

This discussion paper and a companion discussion paper - Governments and the Residential Mortgage Market I: A Normative Analysis (Fallis, 1983b) - were prepared as background studies for the Economic Council of Canada's report on financial markets Intervention and Efficiency (E.C.C., 1982). The purpose of the two discussion papers was to examine government involvement in residential mortgage markets. The work was divided into two parts.

The first part, reported in the companion discussion paper, uses neoclassical welfare economics to specify the appropriate role for government in residential mortgage markets. In the analysis it is assumed that the well-being of society can be measured by the social welfare function. There are a number of reasons why a laissez-faire economy may not achieve the maximum possible level of social welfare; for example there might be non-competitive markets or there might be externalities from consumption or production. There are eight general reasons, in all, why the private market might fail to generate the social welfare maximum and each provides a possible justification for government involvement in the economy. The companion discussion paper applies this normative framework of welfare economics to housing matters in Canada. Each reason for intervention is examined to see whether there is evidence to warrant the involvement of government. For example, evidence is sought on whether Canadian mortgage lending, mortgage insurance and housing markets are competitive. In cases where an intervention might be warranted, the question is then addressed - what is the best government program to deal with the problem? The government has many instruments at its disposal, from regulation to direct expenditures, but the focus in this work is on situations where interventions in the residential mortgage market such as direct mortgage lending or public mortgage insurance will be the best instrument.

The analysis concludes that a government presence in residential mortgage markets is called for, but the government should act as an overseer and participant in certain specific, limited circumstances rather than as a major financial intermediary. Public mortgage insurance should be continued or public re-insurance of private mortgage insurance be instituted in its place. Public mortgage lending should be available as an instrument to use when there are unserviced borrowers because private lenders cannot pool high risk loans or have incorrect information. But before such lending is done, there ought to be a careful examination of the existence and problems of unserviced borrowers. Public mortgage lending might also be used as part of a renovation assistance program designed to increase housing consumption or as part of an optimal fiscal and monetary policy to stabilize the national economy.

These conclusions emerge from applying welfare economics to Canadian housing markets, assuming that governments seek to maximize the social welfare function. The analysis makes no reference to existing government housing programs. The purpose of this discussion paper is to describe the involvement of the federal and provincial governments in Canada in the residential mortgage market and to evaluate the involvement by comparing it with the recommendations of welfare economics.

Chapter 2 describes the mortgage lending and mortgage insurance programs in which the federal government has been involved over the last thirty years, whether alone or as a joint federal-provincial, or federal-provincial-local undertaking. First an overview of federal involvement is provided and then the separate programs are described, detailing the stated rationale of the program and the instrument of intervention. Chapter 3 describes provincial involvement in a similar way, with an overview followed by a more detailed look at the programs in Alberta, Ontario, Quebec and Nova Scotia.

Chapter 4 evaluates this government involvement by juxtaposing the actual programs against the programs recommended in the companion discussion paper. The stated objectives of government housing programs are compared with the welfare economic rationales for government intervention, then the actual instruments of intervention are compared with the optimal instruments recommended by economic theory, and finally the costs of non-optimality are discussed. Chapter 5 concludes the look at governments and the residential mortgage market with a summary of the two discussion papers.

2 PROGRAMS OF THE FEDERAL GOVERNMENT

The federal government in Canada has been extensively involved in housing matters since the Second World War, which led to involvement in the mortgage market of two principal sorts: direct mortgage lending and mortgage insurance.[1] The purpose of this chapter is to outline federal housing programs which involve the residential mortgage market. The emphasis will be on programs under which insurance or mortgage loans have been provided recently. However, this would not be a complete picture. Several major programs that have been amended or curtailed over the years account for a substantial portion of loans outstanding and imply significant ongoing subsidies to households already in the programs. Although new loans are not being made, these programs constitute part of present policy. Therefore the chapter will also discuss briefly the historical evolution to the current state of affairs. Any program in which the federal government participates will be considered here as a federal program, although it may be a joint federal-provincial or federal-provincial-local undertaking. The next chapter will describe purely provincial or provincial-local programs.

There have been many, many, housing programs over the last thirty years and near constant revision of ongoing programs. Any summary discussion is greatly facilitated by a typology to group the various sorts of policies. There exist several ways to type housing programs - for example, according to whether they principally influence ownership or rental markets, according to the income class of the nominal beneficiaries, according to the rationale of the program or according to the instrument used to effect the program. The companion discussion paper - Governments and the Residential Mortgage Market I: A Normative Framework - provided an economic analysis of housing policy emphasizing the rationale for intervention and the choice of instrument. In Chapter 4 of this paper, existing programs will be juxtaposed against the approach of economic theory. To facilitate this, federal and provincial housing programs will be characterized according to the instrument of intervention.

This typology is, in some ways, unsatisfactory. It would be ideal to begin from the objectives or rationale for the program. However, it is extremely difficult and often impossible to discover the government's rationale for programs. The sources for such information - the enabling legislation, the statements of cabinet ministers or government publications describing the programs - usually reveal extremely general statements which are of little assistance in designing a typology or in assessing whether the program meets its objectives. For example, the rationale or purpose of a program might be to "supply decent low-rental accommodation for the elderly." The program will meet the objective in an almost tautological sense because the objective is merely a statement of what the program does. The characterization of programs according to the instrument used is therefore more feasible and certainly consistent with the focus of this discussion paper.

This chapter is divided into four sections. The first offers an historical overview of federal housing policy emphasizing involvement in residential mortgage markets, the second a description of mortgage insurance programs, the third a description of mortgage lending programs, and the fourth offers brief descriptions of programs pursuing housing-related objectives but which are carried out using other instruments and therefore can be seen as alternatives to direct involvement in mortgage markets. In the latter sections, the instruments of a program are detailed and the stated rationale outlined.

Overview

Federal housing policy, with corresponding involvement in mortgage markets, can be broadly classified into three periods.2 The first, from 1954 to 1964, was concerned primarily with increasing the construction of single detached homes for families of the baby boom. In 1954, a federal mortgage insurance program was instituted under which borrowers paid an insurance premium to CMHC for mortgages obtained from authorized private lending institutions. CMHC would then cover any interest or capital losses of lenders on defaulted loans. CMHC established the terms of loans eligible for insurance, including the interest rate, and therefore exerted considerable influence on the portfolio selection of authorized lenders. Often changing conditions in the financial markets sharply altered the relative attractiveness of such loans, although the government had not changed the terms for eligibility. Table 2-1 shows the annual amounts insured over the period and reveals the fluctuations. The other major program of the period involved the use of public funds for mortgage loans to finance new residential construction. These loans were designed to be residual in the sense of being offered when private sector lenders had rejected a borrower's application. The program made far more than residual loans and often was used to create employment and to stabilize fluctuations in housing construction. Both programs have been central components of federal housing policy since their inception.

The second period, from 1965 to 1977, was concerned with social housing policy. The first initiative was a cost-sharing formula for provincial or municipal public housing projects which would be rented to low-income families and the elderly on a rent-geared-to-income basis. The new arrangements drew the provinces for the first time extensively into the housing area. The public housing program grew rapidly, until by 1971 it advanced $271 million in loans, accounting for almost 30 per cent of CMHC's lending (see Table 2-2). There followed a series of programs - Entrepreneurial Housing, Non-profit Housing, the Assisted Rental Program - all basically intended to provide moderately-priced rental housing at slightly less than market rates. Thus the purview of social housing policy expanded beyond low-income to middle-income renters. In 1973, it expanded yet again with the offering of substantial assistance to middle-income, first-time home buyers under the Assisted Home Ownership Program (AHOP). The Residential Rehabilitation Assistance Program provided mortgage loans and grants for the renovation of owner-occupied and rental premises. In 1975, at the height of this expansion, CMHC advanced over $1.6 billion in loans under all of its various programs.[3]

The major programs begun earlier also continued during the second period (see Table 2-2). The mortgage insurance program gradually evolved, under criticism of how CMHC established the interest rate, until in 1969 the NHA mortgage rate was freed to be established in the private financial market. The other terms of the loan however are still set by the government. Direct lending continued as a major undertaking until 1973 when it was replaced by AHOP, although its character changed after 1968 when the lending was directed more toward financing housing suitable for low and moderate income households.

The final period, from 1978 to the present, was one of significant restraint (see Table 2-3). The programs assisting middle-income renters and home buyers were halted, and the public housing program was cut back. The federal government provided only $327 million in loans in 1980 (compared to $1.6 billion in 1975), and encouraged those agencies wishing to utilize the remaining social housing programs to secure private sector loans which could then be insured under the NHA. Mortgage insurance remains, although private insurers now exist; and the assistance for rehabilitation continues. In 1982 several major programs to stimulate the construction of single family dwellings and apartments and the renovation of the existing stock were implemented. Although of significant impact on the housing sector, they were primarily motivated by concerns of macroeconomic policy. By mid 1983, the programs had been terminated. It is of course uncertain whether new housing initiatives will emerge.

In summary, federal housing policy began by encouraging the construction of single detached housing, then expanded into income redistribution programs but in recent years contracted, restricting its focus to mortgage insurance, social housing for rural and native groups, and housing rehabilitation.

Most of the programs, as will be detailed in the remainder of the chapter, attempted to provide housing at less than market prices to participants through a combination of loans and grants. The mortgage loans were often at interest rates below those in the private market and with other more generous terms such as higher loan-to-value ratios and longer amortization periods. The grants sometimes covered part of initial capital costs and sometimes were of a continuing nature to offset operating losses on apartment units or to subsidize a home purchase over time. From the borrowers' perspective, loans on generous terms and grants are substitutes for one another.[4] The criteria governing the choice between the instruments has never been very clear. There does seem to be the political perception that a grant is somehow more of a subsidy than an attractive loan.

The mortgage insurance provided was of two sorts, although CMHC never clearly distinguished between them. Until the mid-seventies the insurance provided was actuarially sound, with the premiums paid by the borrowers sufficient to cover costs and any claims. Such insurance could be provided by the private sector and indeed there is now private mortgage insurance in Canada. Recently CMHC offered insurance on loans by private lenders made under social housing programs, particularly AHOP and the Assisted Rental Program. These loans were considerably more risky than regular mortgage loans but there was no adjustment in the premiums. In effect, assistance was provided by reduced insurance premiums. This is a further substitute for attractive loans, but again the criteria governing the choice of instrument was never identified.

These housing activities are a significant part of government financial intermediation in Canada and therefore also of overall intermediation because governments account for 23 per cent of total intermediation and are the second largest intermediary after the chartered banks (E.C.C., 1980, Table 3). The assets of CMHC were $9.835 billion at the end of 1977, representing over 11 per cent of total government assets from financial intermediation in Canada, ranking CMHC just behind the Bank of Canada and the Canada Pension Plan in importance, in terms of assets, as a government intermediary (E.C.C., 1980, Table 2 and Table 6).

The relative importance of these lending and insurance activities in Canadian housing markets can be seen in Table 2-4 and Table 2-5. The loans advanced by CMHC were the principal source of financing for at least 10 per cent of Canadian housing starts in each year between 1965 and 1975 and were as high as 30 per cent in 1970.[5] The importance has declined significantly since 1975 and by 1982 less than 2 per cent of starts were financed by CMHC loans. Loans by approved lenders insured under the National Housing Act financed an additional at least 20 per cent over most years.

Table 2-5 shows the importance of CMHC in total mortgage lending. CMHC until 1975 accounted for 10 per cent of lending almost every year but since then the percentage has fallen sharply to well below one per cent. Loans insured under the NHA show considerable annual variation but still represent almost 30 per cent of all mortgage loans.

There can be little argument that the federal government was until recently a major financial intermediary in the financing of housing. It remains as the major provider of mortgage insurance, a lender of last resort and as a lender for housing rehabilitation and public housing financed under the federal-provincial program. It also has a new non-profit program but is is unclear how much public lending will be involved because private groups seeking to use the program must first try to obtain private funds.

The remainder of the chapter provides greater detail about these activities. The following section examines mortgage insurance and the subsequent section, mortgage lending programs. The discussion will present the objectives of each program, the form of assistance and a few comments about how the program has evolved over time. This is a large amount of rather dry detail and readers may omit these sections with no loss of continuity and refer to them for more information when the programs are mentioned in other sections of the discussion paper. The chapter concludes by examining several housing-related programs which have involved financial intermediation and programs which are substitutes for mortgage lending and mortgage insurance in that they pursue the same goals using different instruments.

Mortgage Insurance Programs

A cornerstone of Canadian housing policy has always been the public provision of insurance on mortgage loans by approved lenders. NHA Mortgage Loan Insurance was intended to make mortgages a more attractive investment for financial institutions, thus increasing the flow of mortgage credit, reducing mortgage interest rates and liberalizing the terms of mortgages. In turn, this would stimulate demand and increase residential construction. Until 1954, the federal government guaranteed loans made jointly with approved lenders. This was replaced in 1954 by the public insurance which remains today. On behalf of the mortgage insurance fund, CMHC insures the approved lender against loss through borrower default. The loan application fee and insurance fee (about 1 per cent of the loan) are paid by the borrower to CMHC. The insurance fee is added to the mortgage and amortized with the loan (CMHC, 1976b, 1). CMHC establishes the criteria for eligible loans. A maximum loan is set, differing by region; the term is established, usually 5 years with an amortization period of from 25 to 40 years; loan-to-value ratios may be as high as .95 for mortgages financing home purchase; and principal interest and property taxes cannot exceed 30 per cent of the borrower's allowable gross income. The maximum allowable loans are rather low and in major metropolitan areas are well below the average house price so NHA insured financing is mainly used for condominiums and townhouses. The interest rate is now free to be established in the financial markets, although this was not always the case. Until 1966, the rate on NHA insured mortgages was set by the government provided the rate was not more than 2-1/2 per cent above the government long term bond yield (Smith, 1974, 7). The balancing of borrower pressure to reduce interest rates against the realities of the financial markets, which required mortgage rates to increase with other rates if the supply of mortgage credit was to be maintained, was not an easy task for the government. From 1966 to 1969, the mortgage rate was tied to the average yield on long-term government bonds of the previous quarter. The maximum NHA rate was first 1-1/2 per cent and then 2-1/4 per cent above this bond yield (Smith, 1974,7). In 1969, the rate was freed.

From the beginning of public insurance, the majority of NHA insured loans were used to finance the construction of new detached single family houses (the mortgages were then assumed by the purchaser). In 1959, loans for rental construction were eligible and in 1969 loans to finance purchases of existing housing became eligible. During the 1950's life insurance companies and chartered banks were the main source of funds; in the 1960's trust companies emerged as a major source; and in the 1970's banks and trust companies increased their involvement while the share of life insurance companies showed a decline.

The insurance program contained no subsidy element for most of its operation. The insurance fund maintained adequate reserves for the insurance in force (CMHC, various years, 1980 Table 30). However, the origination fee has in recent years been well below actual costs; the difference being covered by general revenues rather than the insurance fund (Task Force, 1979, 77). Whether an implicit subsidy has been in effect is difficult to establish, although it is clear the insurance premium is below what financial institutions impute for self-insurance on conventional loans (Smith, 1974, 141) and now is below what private insurers believe to be an appropriate premium.

There also has been a significant change in the last five years. The federal government has attempted to reduce its mortgage lending and at the same time to continue many of its housing assistance programs. Private mortgage loans made to persons and organizations under assistance programs, for example those receiving AHOP subsidies or non-profit groups receiving interest reduction grants, have been insured. In addition, graduated payment mortgages are now insurable. The insurance premium has not been adjusted to reflect the increased riskiness of such loans, resulting in a significant subsidy. The mortgage insurance fund has had net outflows of hundreds of millions of dollars during 1979 and 1980 (in part offset by the acquisition of houses) as these high risk loans defaulted. A clear separation of risk classes and identification of implicit subsidies on insurance premia for each class has not yet been achieved but is obviously required.

A second insurance system, NHA Home Improvement Loan Insurance, also has always been a part of housing policy. It is intended to promote the modernization and repair of existing houses (CMHC, 1976b, 20). Insurance is available on loans, often secured as a second mortgage, made by approved lenders to be used for home improvements. It is available on loans to homeowners or owners of rental property at a premium of 1 per cent of the loan, payable by the borrower. Loans cannot exceed $4,000 for a one family dwelling, or $4,000 on the first unit and $1,500 on each additional unit of a multiple family dwelling. The program does not appear to involve a subsidy with the insurance fund covering costs and maintaining adequate reserves against insurance in force (CMHC, various years, 1980 Table 30). A small but steady flow of loans was insured until the early 1970's when a decline began. In the last several years federal and provincial subsidies have been available for home rehabilitation and the decline has been very steep.

Mortgage Lending Programs

The Direct Lending Program is intended to make available mortgage loans for the purchase of new or existing housing to applicants who are unable to obtain loans from approved lenders. It has sometimes been called residual lending, but has been used more generally to stimulate construction. The maximum loans are the same as NHA insured approved lender loans: 95 per cent of the first $47,000 and 75 per cent of the balance subject to maxima which vary by location. In major metropolitan areas these maxima have meant that lending has financed mainly condominiums and townhouses over the last few years. The term of the loan is five years and may be amortized over periods of 25 to 40 years. The interest rate applied to the loan is normally at or slightly below the approved lenders NHA rate. Loans on new houses are usually advanced to builders over the construction period and then assumed by the household purchasing the house. Those eligible for assistance must provide evidence (usually in the form of two letters of refusal) that they are unable to obtain approved lender financing (CMHC, 1976b, 2).

In the early 1950's, loans given out under the program were to limited-dividend housing corporations and primary industries which were interested in the construction of rental accommodation for their employees (CMHC, 1954b, 19). Later the lending was used to increase housing starts, especially during the housing cycle troughs of 1958-59 and 1964-67. From 1968 to 1972, the program made loans for new construction with emphasis placed on financing housing for moderate income households. Then, gradually, it returned to its role as a residual lender. Now few loans are made.

The Entrepreneurial Housing Program was designed to increase the amount of moderately priced rental units available. Under this program CMHC provided loans covering up to 95 per cent of the project's lending value, at below market interest rates with a term of up to 50 years. Assistance was available to corporations, organizations and individuals who in return would agree to controlled rents which could be altered only with the permission of CMHC. Before 1968 there were limits on the incomes of persons eligible to live in these projects but the limits were not enforced and often were waived to reduce vacancy rates in an apartment building. In the event of a borrower's failure to maintain the project's low rental character or committing a breach of contract, CMHC could declare the unpaid principal of the loan due or increase the interest rate on the unpaid balance of the loan. Loans could be used either for the construction of a low rental housing project or for the purchase and conversion of existing buildings into a low rental housing project. The program was known before 1967 as the limited dividend program because the terms of the assistance contained an explicit limit on the returns which a landlord could earn. The same result however is achieved with controlled rents given actual costs of operation.

During the late 1960's, the program was criticized as an instrument for providing housing assistance. Buildings often were situated in outlying areas and the majority could not accommodate families with many children. The allocation of units favoured childless couples. Due to such problems and with greater government involvement in low income housing assistance through public housing, non-profit and co-operative housing, CMHC reduced funding for entrepreneurial housing. No loans have been advanced under the program since 1978.

In March 1979 the National Housing Act was amended, significantly changing the programs providing housing assistance to low and moderate income households for rental accommodation. Previously, CMHC had three programs: Public Housing, Non-Profit Housing and Co-operative Housing. These were replaced by a single set of arrangements available to provincial and municipal non-profit corporations, private non-profit organizations and non-profit co-operatives under which CMHC would insure privately arranged mortgages and would provide interest reduction grants. The new arrangements are detailed below under the heading Non-Profit Housing Assistance. The other three programs will then be described because they represent the approach to providing housing assistance over the last twenty years (and hundreds of thousands of units under these terms are part of our housing stock). The terms offered under the Federal-Provincial Housing Program for financing public housing remain available.

The reasons for these revisions are several, but most importantly the revisions sought to reduce federal lending, to increase reliance on private mortgage markets as a source of funds, to increase provincial and municipal responsibility for the initiation and management of assisted housing, and to produce housing in which households receiving rent-geared-to-income assistance would be mixed with other tenants. The revisions represent a key aspect of the federal restraint in the housing field, especially restraint in mortgage lending.

Non-Profit Housing Assistance is designed to assist non-profit housing organizations in supplying low and modest cost rental accommodation for families and individuals. Both capital and operating assistance are available under the program. Capital assistance entails NHA insurance on mortgage loans from NHA approved lending institutions for up to 100 per cent of the lending value of the project. This likely involves a subsidy because the insurance premium does not reflect the riskiness of these loans compared to other loans insured under the NHA. CMHC will also offer second mortgages for the last 10 per cent of lending value and be a lender of last resort for private non-profit and co-op groups. Operating assistance is available in the form of an annual federal interest reduction grant which helps offset operating losses. The maximum grant has the effect of reducing the effective interest rate to two per cent over a 35-year loan amortization period. The assistance has two components. The first permits rents on the buildings to be set at the lower range of market rents on comparable buildings in the area. Therefore there is a subsidy, often a substantial one, to all households in the building. The second component permits some of the units in a building to be rented to tenants on a rent-geared-to-income basis. Some provincial governments offer an additional grant, if required, of up to 100 per cent of the federal grant.

If the above assistance is insufficient to meet all operating losses of municipal non-profit corporations, the federal and provincial governments contribute additional assistance on a 50:50 ratio. Private non-profit and co-operative groups are eligible to receive start-up grants of up to $75,000 (CMHC, 1978b).

Criteria for approval of loans include evidence of need for the project, capital costs which are within federal maximum unit price guidelines and the provision of both market and rent-geared-to-income components. Up to 25 per cent of the units in a municipal non-profit development for families may be allocated on a rent-geared-to-income basis, while in senior citizen projects up to 50 per cent of the units may be assigned to those in need of rental assistance.

The Public Housing Program was created to provide adequate low cost rental accommodation for families and individuals unable to obtain such accommodation at prices they could afford. The assistance is provided in two ways. Federal-provincial housing involves a partnership agreement between the federal and provincial governments in which the federal government provides 75 per cent of the capital cost and operating losses. The provincial government provides the balance, but may request a municipality to assume a portion of the provincial share. These terms have been available since the Second World War. Because the program required joint ownership rather than outright provincial ownership of public housing projects the program remained small in the early period, and then was dominated by the public housing terms which became available in 1964 (see Table 2-1 and Table 2-2). However since the late 1970's it has been more utilized. It is used mainly by Newfoundland, Nova Scotia and Saskatchewan.

The alternative public housing terms under the 1964 NHA amendments constituted what is normally termed public housing and involved CMHC loans to provincial or municipal agencies which would manage the public housing projects. The new terms proved popular leading to the creation of provincial housing bodies and the explosion of public housing construction in the late 1960's and early 1970's. They mark the beginning of a significant provincial role in housing policy. Construction or acquisition loans for up to 90 per cent of the total cost of the project are available. The term of the loan may be for as long as 50 years at a preferred interest rate, sometimes as much as 2 percentage points below the private mortgage rate. Provinces supply the remaining 10 per cent of capital costs. The federal government provides 50 per cent of the annual operating losses incurred in the operation of public housing projects; the other 50 per cent is provided by the province, or the province and the municipality in which the project is located (CMHC, 1976b, 8). This program is now available only for a transition period following the establishment of the new non-profit program.

Projects must meet certain criteria in order to receive assistance. There must be evidence of a need for low rental housing such as over-crowding, or substandard housing; buildings must meet certain standards, for example regarding the availability of community facilities; and projects must have provincial approval. Tenants are charged a rent geared to their income, usually about 25 per cent of their income although the lowest income tenants pay a lower percentage. Most tenant households are families or senior citizens. Public housing was heavily criticized for creating ghettoes of the poor and was curtailed in the late 1970's, especially public housing for families. Recent initiatives in housing assistance have emphasized mixing tenants of various income groups. However, this has often meant higher income households also receive subsidies.

The Co-operative Housing Program aided low and moderate income persons organized in a co-operative to obtain housing which would be owned by the occupants either individually or collectively. Continuing co-operatives, in which the members jointly own the housing units and occupy the units of their choice under a lease agreement, could obtain a mortgage for 100 per cent of the total lending value of the project, at a preferential interest rate, and with a maximum amortization period of 50 years. A 10 per cent capital contribution was also provided. Building co-operatives, in which houses are co-operatively constructed but owned individually by the members, could receive a 95 per cent loan with a 35 year term at an interest rate as low as 8 per cent plus an annual contribution of up to $750 towards payment of interest, municipal taxes and repayment of the loan (CMHC, 1976b, 5). These terms were a modification of the AHOP program to suit a co-operative approach.

Groups eligible to receive assistance must be registered as a non-profit continuing co-operative with a minimum of 51 per cent of the continuing co-operative project's occupants being members.

Co-operative housing has existed in Canada since the early 1930's, for the most part in the Maritimes. During the 1950's and 1960's, co-operative housing projects were built across Canada. Assistance was always available from CMHC, but no one section of the NHA specifically dealt with assistance for co-operatives. The terms described above relating to co-ops were introduced in 1973.

Now co-operatives may receive the same assistance as any non-profit group.

The Non-Profit Housing Program was intended to increase the supply of rental housing for low and moderate income families, the elderly and special groups such as the handicapped. Mortgage loans were available to non-profit organizations to cover 100 per cent of the lending value of a building project, over a 50 year amortization period, at an attractive interest rate. In addition, non-profit borrowers could receive a 10 per cent capital grant; and start-up funds to a maximum of $10,000 were available to the sponsors of a private non-profit housing project (CMHC, 1976b, 6).

To qualify, groups must be constituted as exclusively charitable, non-profit organizations which may be either organizations where all the shares or capital are owned by a province or municipality, or organizations constituted exclusively for charitable purposes. Financing was made available for the construction of new housing, to purchase existing housing already accommodating low income persons who were facing dislocation or for the rehabilitation and conversion of existing housing which would increase the number of housing units.

Non-profit housing had existed in Canada for a long time without government assistance. The subsidy system emerged because it was felt that non-profit groups (and co-ops) would more effectively manage assisted rental housing projects for low and moderate income households than would private entrepreneurs. As a result, a special section of the National Housing Act was provided to deal with non-profit groups in 1973, while assistance to entrepreneurs was phased out.

The Rent Supplement Program was begun in 1971 to permit the provision of continuing housing assistance to low income households outside public housing projects, in buildings with tenants of many income levels. Assisted households pay a rent according to their income, just as in public housing, but live in privately owned, non-profit owned or co-operative housing. The difference between the market rent and actual rent paid is shared 50 per cent by CMHC and 50 per cent by the province and municipality. Often, a province would sign an agreement with a private landlord to make units available to tenants from public housing waiting lists; or lending under the Non-profit and Co-operative Programs would be combined with rent supplement arrangements. In no case could more than one quarter of the units in a building have rent supplement tenants. The program has remained small and has been largely superseded by the new non-profit program which offers interest reduction grants to permit rentals to low income households.[6]

The Student Housing Program was devised to increase the supply of housing for students. It assisted those agencies which were involved in the construction, acquisition or improvement of a student housing project, or in the acquisition and conversion of existing buildings into student housing. Mortgages were made available for 90 per cent of the cost, up to a maximum amount, for a 50 year period at interest rates below the market rate. Those qualifying for assistance included a province, municipality or their agency, a hospital, school board, university, college, co-operative association or charitable corporation. However, the respective provincial government must approve the making of the loan (CMHC, 1976b, 11). Prior to November 1966, university housing projects were the only educational institutions that CMHC could assist, and even after eligibility was broadened most of the lending has been for university residences. There has been little lending under the program since 1972.

In the years up to 1974, inflation had increased significantly as had house prices, rents and interest rates. Between 1973 and 1974 housing starts fell sharply. There was a widespread belief that Canada faced a housing crisis. More in response to the pressures of the moment than a careful examination of the situation, the federal government initiated two major subsidy programs - one to stimulate construction of moderate priced homes begun in 1973, and one to stimulate moderate priced rental housing begun in 1976. The subsidies under both were terminated in 1978 when the terms were changed to offer only a form of graduated payment mortgage which the government hoped would soon be available from private lenders.

The Assisted Home Ownership Program (AHOP) was devised to encourage the production of moderately priced housing for homeowners. Under the original 1973 version of AHOP, CMHC provided a mortgage of up to 95 per cent of the lending value of the house, for a five-year renewable term with amortization of 35 years. CMHC would then reduce the interest rate from that written on the mortgage down to eight per cent or until payments of principal, interest and taxes reached 25 per cent of income. If payments still exceeded 25 per cent, a grant of up to $300 per year was available to reduce monthly payments to the 25 per cent figure (by June 1975 this grant had been increased to $600 per annum). Those eligible for assistance had to have incomes below a certain level, had to be purchasing a house priced below a certain level which varied by city, and had to have one or more dependent children (Ontario, 1975).

A 1976 revision of AHOP offered an interest reduction loan rather than a grant, to bring the interest rate to 8 per cent and used private first mortgage money. Annual loans were available in the first five years of occupancy and were interest free. The initial amount of the loan was reduced by one-fifth each year. The loans were a second mortgage on which payments began after five years. Immediate repayment was required if the property was sold or if a new first mortgage was obtained for an increased amount. If purchasers made use of the maximum interest reduction loan and had at least one dependent child and were still paying more than 25 per cent of their gross household income on mortgage payments and municipal taxes, they were eligible for an AHOP subsidy. The maximum subsidy was $750 in the first year of occupancy, then reduced over five years. Often provinces offered still further assistance to permit relatively modest income households to purchase a home.

In 1978, AHOP was scaled down still further. The subsidy was removed leaving only a payment reduction loan which had the effect of converting payments under this program and a regular first mortgage into a graduated payment mortgage. The payment reduction loan was an interest-bearing second mortgage which in the first year of ownership provided the borrower with an amount equal to $2.25 per month for every $1,000 of the borrower's first mortgage. The amount of the second mortgage advanced was gradually reduced at a rate which produced a constant five per cent increase in the borrower's mortgage payments. The loan advances continued for five years at the end of which the full amount of the loan became repayable with interest calculated from the date of the initial advance of the loan. These loans were available for a transition period until private lenders offered graduated payment mortgages which had become insurable under the National Housing Act. No loans are now made under AHOP.

The Assisted Rental Program (ARP) provided financial assistance to developers of moderate and low priced rental housing enabling them to charge rents comparable to existing buildings rather than rents which would be required given the current interest rates and costs. In 1975, the program offered cash subsidies. By 1976 this was revised to a system of assistance loans secured as a second mortgage. The maximum annual loan was $1,200 per unit and interest free up to 10 years. The loan was decreased by one-tenth of the original amount each year. The rate of interest payable on the loan at the end of 10 years was the NHA direct lending rate. This whole process could be extended to 15 years depending on the cash flow of the entrepreneur. This assistance was recoverable upon sale or refinancing (CMHC, 1976b, 4).

The 1978 version of the program provided payment reduction loans, secured as a second mortgage, not exceeding, in the first year an amount equal to $2.25 per month for each $1,000 of the first mortgage. The loan bore interest at the same rate as the first mortgage, which had to be insured under the NHA and not more than 90 per cent of the project's cost as determined by CMHC. The amount of the second mortgage advance was gradually reduced at a rate producing a constant five per cent increase in the borrower's net principal and interest payments annually. As with AHOP, the 1978 revisions had the effect of creating a graduated payment mortgage. It was hoped private lenders would soon offer such loans removing the need for public intervention.

The Residential Rehabilitation Assistance Program (RRAP) was begun in 1973 and provides assistance, through loans and grants, for the repair, rehabilitation and improvement of substandard housing inhabited by people of low and moderate income in designated areas (Neighbourhood Improvement Areas). CMHC lends homeowners up to $10,000 per dwelling unit, $5,000 of which may be forgiven at a rate of $1,000 for each year the homeowner occupies the dwelling. Homeowners with adjusted family incomes up to $13,000 are eligible for the maximum forgiveness, while those earning $23,000 or more must repay the loan in full. Owners of private rental property suitable as family housing using an NHA insured loan for renovation are eligible for forgiveness of up to $3,500 for each family housing unit or $2,500 for each unit of hostel or dormitory accommodation in return for maintaining 'fair rents.' Non-profit corporations and co-operatives can also obtain loans, with up to $5,000 forgiven. The levels of assistance and income cut-offs for maximum assistance have been raised over the years of the program.

In order for a dwelling unit to receive assistance it must be substandard and capable, after rehabilitation, of providing at least 15 years further use. RRAP is operated on the basis of annual agreements with the provinces. The agreement contains a provincial allocation of funds for re-allocation amongst municipalities selected by the province and accepted by CMHC. Municipalities in turn, select neighbourhoods for participation in the program. In 1979, amendments to the NHA allowed private lending, insured under the NHA, to replace public loans to landlords under RRAP. In recent years, the program has seen heightened activity as a result of an increase in the income limits for homeowners eligible for loan forgiveness.

In late 1981 and 1982, several mortgage market programs were introduced which have since become inactive. All were designed as short term interventions to deal with a specific problem. One was to deal with homeowners who had to renew their mortgage at high rates of interest. The other three were intended to stimulate housing construction and renovation as part of a macroeconomic policy designed to stimulate the economy and to create employment. Clearly macroeconomic policy issues explained these interventions rather than housing policy issues. In some cases there was no income limit on eligibility for assistance. Many of the mortgage lending programs already described have been used from time to time as instruments of macroeconomic policy, especially the direct lending program. The amount of money which the government was willing to lend at any time would be set by macroeconomic concerns. The recent programs represent something of a change because the instruments themselves were designed largely with macroeconomic policy in mind.

The Canada Mortgage Renewal Plan was intended to assist homeowners who faced financial difficulty when they had to renew their mortgages at high interest rates. There was a guarantee to lenders who deferred interest payments and grants to owners of up to $3,000 to bring annual payments down to 30 per cent of income. Later the deferred interest provision was removed and the program worked as a pure grant.

The Canada Rental Supply Plan provided interest free loans for 30,000 rental units in areas of low vacancy rates. The loans were for 15 years and subsequently payable at market interest rates. The Canadian Homeownership Stimulation Plan provided loans and a $3,000 grant to purchasers, regardless of their income, of a newly built home or of an existing home if they were first time buyers. The Canada Home Renovation Plan provided homeowners with loans of up to 30 per cent of the cost of renovation to a maximum of $3,000. A minimum of one third of the cost had to be spent on contracted labour. Households with incomes of less than $30,000 could have the entire loan forgiven. The amount of forgiveness was reduced until household income reached $48,000 when the household became ineligible for the program.

Housing Programs Using Alternative Instruments

The focus of this discussion paper is on government mortgage insurance and mortgage lending as a result of housing concerns. The overview section summarized the evolution of federal policy and then the principal programs were described in greater detail. For the sake of completeness,[7] this will be extended to deal briefly with regulation of the mortgage market, other lending programs and income tax provisions pursuing housing objectives. These represent alternative instruments which the federal government has used to pursue the goals of the mortgage insurance and mortgage lending programs.

The federal government has not engaged in regulation of the capital markets to increase the flow of mortgage credit, a remarkable fact given such activities in the United States and Great Britain and Canada's reputation for regulatory intervention to achieve public goals. Indeed the period since 1950 has been marked by a gradual removal of regulations on financial markets and the integration of the mortgage market with other credit markets. The latter was mainly achieved by gradually admitting the chartered banks into mortgage lending. The banks were first permitted to make mortgage loans in 1954 provided the loans were insured under NHA insurance. The 6 per cent rate ceiling on bank lending sometimes curtailed their mortgage lending but this ceiling was removed in the 1967 Bank Act revision. As well, banks were permitted in 1967 to enter the conventional mortgage market, greatly widening the potential source of funds. Banks may only lend up to 75 per cent of the property value but they have mortgage affiliates which supply the remainder up to 90 per cent (Binhammer and Williams, 1976). In 1967, banks were permitted to issue debentures and when the 5 year renewable mortgage became insurable under the National Housing Act in 1969, a matching of the terms of assets and liabilities became feasible. Coupled with the removal of controls on the NHA mortgage interest rate in 1969, a clear pattern of deregulation and increasing competition in the mortgage market is revealed.

As the above paragaph makes clear, the general regulations covering the banking system and also covering the trust and insurance companies affect the overall flow of mortgage credit. Any regulation governing the allowable loans or deposit instruments of these financial institutions which influences the relative attractiveness of loans or deposits will have some effect. Similarly restrictions on the ownership of these intermediaries or regulations covering the fiduciary responsibilities of their officers will have some effect. The Cadillac-Fairview sale and refinancing in Ontario are evidence of these. However, these regulations deal more generally with private financial intermediation and are not primarily designed to influence mortgage credit or housing matters.

The one instrument which has been used to affect mortgage credit is moral suasion. In the mid 1970's, lending institutions were asked to direct additional funds into financing low and moderately priced housing and to provide high ratio lending to such housing (CMHC, 1976c). Recently, banks have been asked to give special consideration to households having to refinance their mortgages at much higher interest rates. These were clear attempts to achieve public policy goals without having to engage in public mortgage lending.

The federal government has not resisted the establishment of a secondary mortgage market but it has only sporadically encouraged it. CMHC has periodically sold some of its mortgage portfolio to private investors and the Residential Mortgage Financing Act of 1973 provided for mortgage investment companies which could hold pools of residential mortgages. The long-called-for Federal Mortgage Exchange Corporation has not yet been established, although the enabling legislation has been passed. As mortgages have shorter and shorter terms, the need for a secondary market has diminished.

More commonly used instruments of housing policy have been public loans to finance urban renewal, land assembly, sewage treatment plants and neighbourhood improvements. Most provinces have programs to support such activities as well. Table 2-6 shows lending by CMHC from 1955 to 1982. Urban renewal loans were used to finance the demolition and clearance of blighted or substandard residential areas for a redevelopment project, usually part of which was public housing. Although the subject of much controversy, the program was never large in Canada. Lending was restricted under the program following the Task Force on Housing and Urban Development (Canada, 1969) and the 1973 amendments to the National Housing Act eliminated all loans for urban renewal. Funds for site clearance became available, however, under the Neighbourhood Improvement Program in 1973 but these have since been discontinued.

The Municipal Infrastructure Program made loans and grants to provinces and municipalities to finance trunk sewers, watermains, and sewage and water treatment facilities (CMHC, 1976b, 12). Always a major program, it advanced over $100 million annually from 1971 to 1978 but now has been stopped altogether. The provision of such services is clearly a natural monopoly which is normally dealt with by having the public sector provide the services. These loans formed part of our system of intergovernmental fiscal arrangements which attempted to balance the revenue raising and borrowing capabilities with the expenditure responsibilities of the various levels of government.

The land assembly program was intended to ensure an adequate supply of serviced residential land, to stabilize and where possible reduce land prices, and to promote a high standard of residential development (CMHC, 1976b, 14). It was often claimed that public land banking could reduce long run land prices but this became muted as it was discovered that land was not supplied monopolistically and that at best public banking could raise prices as the land was acquired and lower prices as the land was sold, while at worst seriously disrupt the land market even raising prices in the long run. Subsequently the more emphasized goals were land use control and the advance acquisition of land for assisted housing. The program was very large for a few years in the mid 1970's but shrank as the federal government shifted responsibility for achieving these goals to the provinces, deferring to a long standing provincial request.

Under the Neighbourhood Improvement Program (NIP) in the 1970's the federal government contributed 50 per cent of the cost of acquiring and clearing land for social or recreational facilities or housing, of constructing social or recreational facilities and

25 per cent of the cost of improving municipal and public utilities in run-down neighbourhoods. Loans were also available for improvement of commercial enterprises.

The final area of federal involvement concerns the special provisions, or tax expenditures, under the income tax system which relate to housing.[8] To the extent that provinces accept the federal definition of taxable income, there are provincial tax expenditures as well. The most important provisions subsidize the ownership of housing and, measured as foregone tax revenue, are far larger than any of the explicit housing programs described in previous sections. The net imputed income from ownership of housing is not taxed, the capital gains realized on the sale of a principal residence are not taxed and savings of up to $1,000 per year and a cumulative total of $10,000 may be deducted from taxable income if contributed to a Registered Home Ownership Savings Plan and used to purchase a house. The Department of Finance (Canada, 1979) estimated the foregone federal tax collections under these three provisions to be $2,500 million, $3,700 million and $115 million respectively. Investment in rental residential buildings also receives special treatment although the foregone revenue is far less (Smith, 1981). Allowable depreciation exceeds economic depreciation and losses from the ownership of certain multiple unit residential buildings (MURB's) may be applied against income from other sources. The trend of tax policy in recent years has been to treat investment in rental residential buildings similarly to other investments, which has tended to make it relatively less attractive (Smith, 1977).

Certain of these tax expenditures are retained for administrative rather than policy reasons but most have been either initiated or retained after scrutiny because of the benefits which accrue to homeowners and renters. They are clearly instruments in pursuit of housing goals and may be seen as substitutes for mortgage programs.

Table 2-1

Mortgage Lending and Mortgage Insurance Activities of CMHC
1954-1964
($ millions)

	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964
Mortgage Lending Programs											
Federal-Provincial Housing	11.1	12.4	4.0	11.1	10.7	7.6	6.2	6.0	4.2	10.8	8.3
Entrepreneurs[1]	16.1	9.9	10.5	30.6	49.2	35.5	11.0	25.5	9.0	14.6	11.3
Other Direct Lending[2]	-	-	-	198.7	324.4	308.6	150.1	237.9	154.3	281.2	345.8
Student Housing	-	-	-	-	-	-	-	9.6	24.2	24.4	39.6
Mortgage Insurance Programs											
Insured Mortgage Loans by Approved Lenders	378.2	600.7	378.5	261.0	510.0	283.0	231.9	439.4	383.9	364.5	330.6
Insured Home Improvement Loans by Approved Lenders	n.a.	27.3	29.7	30.6	39.7	37.5	30.1	42.6	38.0	36.7	36.0

[1] Program was also called Limited Dividend Housing.
[2] Program was also called residual lending.

Source Fallis (1980, 14).

Table 2-2

Mortgage Lending and Mortgage Insurance Activities of CMHC
1965-1977
($ millions)

	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Mortgage Lending Programs												
Public Housing	60.9	114.3	128.5	170.5	235.4	277.0	238.0	199.7	177.4	296.2	350.4	153.4
Federal-Provincial Housing	14.6	34.3	41.0	27.9	29.0	31.5	39.1	51.8	58.1	96.2	99.5	104.8
Non-Profit Corporations[1]				31.0	72.9	79.3	42.9	95.1	124.7	159.0	288.0	157.4
Co-operatives								7.6	19.8	44.4	40.3	62.8
Entrepreneurs	19.9	30.6	86.4	146.0	241.2	231.9	94.7	59.5	74.5	235.2	9.2	5.6
Assisted Home Ownership								133.1	435.2	458.2	80.0	23.7
Assisted Rental											137.5	320.8
Student Housing	53.2	56.6	73.8	55.5	41.0	36.7	14.4	3.8	4.0	0.4	-	7.7
Other Direct Lending	451.1	512.7	251.9	163.1	361.5	202.5	110.0	38.2	39.6	13.6	13.8	10.8
Residential Rehabilitation									4.2	14.9	61.0	101.3
Mortgage Insurance Programs												
Insured Mortgage Loans by Approved Lenders	191.2	355.8	832.2	711.0	937.0	1866.4	2150.4	1930.1	1370.0	3576.5	4461.0	6213.7
Insured Home Improvement Loans by Approved Lenders	35.9	35.2	23.9	22.1	16.9	19.0	19.0	16.2	18.6	15.8	10.5	8.8

[1] Data pooled with Entrepreneurs until 1969.

Source CMHC (various years), [1979, Tables 21, 29, 38], [1975, Tables 29,38].

Table 2-3

Mortgage Lending and Mortgage Insurance Activities of CMHC
1978-1982
($ millions)

	1978	1979	1980	1981	1982
Mortgage Lending Programs					
Public Housing	176.1	21.8	21.6	16.8	14.1
Federal-Provincial Housing	125.7	105.8	113.5	96.0	98.3
Non-Profit Corporations	120.6	4.6	4.9	3.3	0.6
Co-operatives	36.9	2.5	1.4	0.1	0.2
Entrepreneurs	1.9	-	-	-	-
Assisted Home Ownership	1.8	-	-	-	290.9[1]
Assisted Rental	96.2	0.4	-	35.6	165.1[2]
Student Housing	6.4	-	-	-	-
Other Direct Lending	11.0	11.0	12.1	20.4	10.5
Residential Rehabilitation	150.1	124.7	132.9	126.3	149.9
Mortgage Insurance Programs					
Insured Mortgage Loans by Approved Lenders	4455.9	4157.0	3333.4	3107.9	3417.3
Insured Home Improvement Loans by Approved Lenders	4.2	3.8	2.9	1.8	1.0

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[1] This figure includes loans under the Canadian Homeownership Stimulation Plan.
[2] This figure includes loans under the Canada Rental Supply Plan.

Source CMHC (various years), [1982, Table 27].

Table 2-4

Dwelling Starts by Principal Source of Financing
1965-1982

	CMHC Direct Lending		Approved Lenders Insured Under NHA	
Year	No. of Units Financed	Per cent of Total Starts	No. of Units Financed	Per cent of Total Starts
1965	30,670	18.4	24,172	14.5
1966	38,591	28.7	12,438	9.2
1967	42,379	25.8	20,829	12.7
1968	23,700	12.0	48,542	10.6
1969	26,416	12.5	55,645	26.4
1970	56,941	29.9	49,612	26.0
1971	41,442	17.7	87,802	37.6
1972	36,939	14.8	96,033	38.4
1973	29,027	10.8	75,469	28.1
1974	30,363	13.7	31,046	14.0
1975	41,800	18.1	47,132	20.4[1]
1976	24,087	8.8	93,883	34.4
1977	17,819	7.2	102,462	41.7
1978	14,760	6.5	72,254	31.7
1979	10,023	5.1	38,680	19.6[2]
1980	3,720	2.3	28,921	18.2
1981	2,148	1.2	26,389	14.8
1982	1,577	1.3	30,577	24.3

[1] Under the AHOP and ARP programs from 1975 - 1978, builders used private financing insured under the NHA but also received direct assistance from CMHC. This lending differs from the usual approved lender insured lending.

[2] Since 1979 the social housing programs have used private NHA-insured loans.

Source CHMC (various years), [1979, Table 14], [1980, Table 14], [1982, Table 14].

Table 2-5

New Residential Mortgage Debt Issued by Source
1965-1982
($000)

	CMHC Direct Lending		Approved Lenders Insured Under NHA		Conventional Loans	
Year	Loans	Percentage of Total Mortgage Debt[1]	Loans	Percentage of Total Mortgage Debt[1]	Loans	Percentage of Total Mortgage Debt[1]
1965	487,470	19.8	320,179	13.0	1,651,108	67.2
1966	555,462	31.0	191,276	10.7	1,044,895	58.3
1967	715,576	29.0	355,844	14.4	1,399,993	56.6
1968	492,316	17.2	832,212	29.1	1,534,267	53.7
1969	606,215	20.4	710,978	23.9	1,651,413	55.6
1970	913,816	30.1	937,046	30.9	1,182,771	39.0
1971	713,294	15.7	1,866,414	41.1	1,962,993	43.2
1972	503,550	9.3	2,150,414	39.8	2,750,134	50.9
1973	479,530	6.4	1,930,122	25.9	5,040,411	67.7
1974	895,643	13.1	1,369,993	20.0	4,589,664	67.0
1975	1,208,409	11.7	3,576,482	34.6	5,561,067	53.7
1976	654,157	6.0	4,461,014	41.1	5,741,264	52.9
1977	365,010	2.4	6,213,661	41.5	8,395,802	56.1
1978	289,607	2.0	4,455,865	31.4	9,440,619	66.6
1979	19,617	0.1	4,156,991	29.5	9,901,608	70.3
1980	19,620	0.2	3,333,408	27.9	8,577,831	71.9
1981	28,864	0.3	3,107,855	33.7	6,082,005	66.0
1982	21,541	0.2	3,417,335	32.0	7,256,293	67.8

[1] Total debt is debt issued by CMHC and lending institutions, which is not all mortgage debt.

Source CMHC (various years), [1975, Tables 33, 38], [1979, Tables 33, 38], [1980, Tables 32, 37], [1982, Tables 32, 37].

Table 2-6

Other Lending Activities of CMHC
1955-1982
($ millions)

Year	Urban Renewal	Land Assembly	Sewage Treatment	Neighbourhood Improvement
1955	1.8			
56	3.5			
57	1.1			
58	0.0			
59	3.4			
1960	4.5			
61	2.9		39.5	
62	3.5		43.4	
63	3.7		35.9	
64	10.3		26.2	
65	n.a.		n.a.	
66	1.1		34.1	
67	9.4		31.2	
68	6.6		39.5	
69	14.5	17.2	50.2	
1970	4.0	24.5	77.7	
71	15.0	21.3	113.7	
72	13.4	74.4	114.8	
73	0.8	185.2	153.8	
74	-	101.4	171.9	3.0
75	0.7	80.2	183.3	10.6
76	0.1	86.4	302.6	17.5
77	-	44.3	247.0	15.4
78	4.1	32.2	290.3	16.2
79	-	17.5	2.6	-
1980	2.2	12.0	10.1	-
81	-	10.0	3.3	-
82	-	6.6	-	-

Source CMHC (various years).

Chapter 2: Notes

1 These activities imply a further involvement in financial markets, namely the borrowings to finance the mortgage lending and the financing of any losses on mortgage insurance which perhaps may involve borrowing. In describing federal programs, the financing side has been ignored because Canada Mortgage and Housing Corporation borrows from the government rather than directly from the private capital market. In any analysis of the effects of these programs, however, the financing must be considered simultaneously.

2 There are numerous surveys of Canadian housing policy available; for example Canada (1962), (1969); Dennis and Fish (1972), Fallis (1980), Rose (1969) and (1980), Smith (1974) and (1977) and Task Force (1979).

3 Under many of the programs of CMHC, the provinces also contributed loans and therefore total public sector lending was even greater than Table 2-1 and Table 2-2 indicate.

4 There are of course some limitations on the substitutability. Grants can offer larger net benefits (unless loans have negative interest rates) and there can be important differences in the distribution of benefits over time.

5 Total federal involvement in housing starts is somewhat larger than this because of direct lending and actual building by departments and agencies other than CMHC.

6 The Non-Profit and Co-operative Programs provided public loans at high loan-to-value ratios. Often up to 25 per cent of the units were assigned to tenants from public housing waiting lists. The units were rented on a rent-geared-to-income basis and the operating losses were shared under the Rent Supplement Program in the same manner as losses under the Public Housing Program. The Rent Supplement Program continues. It is the combination with the other two programs which has been replaced by the new non-profit terms.

7 An exhaustive treatment would describe the housing programs of other departments of the federal government - housing for veterans, defense personnel and rural and native housing - but none involves major public lending (see CMHC (1976b) for descriptions). Also the income security system which transfers income and so permits increased consumption of housing must also be recognized (see C.I.C.S. (1980) for a description).

8 A more complete description and analysis of the tax treatment of housing is available in Aaron (1972), Fallis (1980), and the Canadian Tax Foundation (1973), (1977).

3 PROGRAMS OF THE PROVINCES

An independent provincial role in Canadian housing policy has emerged only relatively recently. It was not until the 1970's that most provinces moved beyond joint federal-provincial undertakings to mount programs of their own. The federal and provincial levels will likely play more equal roles in the 1980's. The 1979 amendments to the National Housing Act and recent program cancellations show clearly that the federal government wishes to change the arrangements under which federal and provincial programs had been operating and to shift responsibility to the provinces in many areas. This chapter examines the evolution to the present of provincial housing activities. First an overview sketches the broad patterns of change and the current situation. Then four sections follow taking a more detailed look at Alberta, Ontario, Quebec and Nova Scotia. The emphasis is on mortgage lending programs which arise in housing policy, their rationale and the mechanism for providing assistance.

Overview

It is perhaps an impossible task to summarize satisfactorily provincial activities of any sort. The voices of the regions are constantly reminding us of their differentness and resisting attempts to define the average situation. In housing, this is further complicated because there is no clearing house gathering comparable data or program descriptions and almost no secondary sources dealing with the provinces or a single province. Notwithstanding these problems, an attempt will be made to describe briefly provincial residential mortgage lending programs.

As a preliminary, it is worthwhile to consider the allocation of responsibility for housing policy under the British North America Act. The distribution of powers followed the general principle that those areas of general interest were allocated to the federal level while those of particular or local interest were assigned to the provinces (Dawson, 1964, 82). Basically, Ottawa is responsible for legislation concerned with finance and banking, trade and commerce, defense, national services (post office and census taking), criminal law and international trade and relations, and more generally, for legislation to assure peace, order and good government. Provincial responsibilities are for hospitals, prisons, education, local works and property and civil rights. Not surprisingly, housing policy is not mentioned explicitly but a reading of the Act would suggest that both the federal and provincial levels would have a major role. The federal government's position follows from responsibility for mortgage markets as part of banking and finance and responsibility for national standards and income redistribution which has been presumed to flow from the peace, order and good government clause. The provincial position follows from housing being of a local nature and from the responsibility for property rights. One would have expected the two levels to be roughly equal partners in housing matters. However, this has not been the case.

The three periods identified in the overview of federal housing programs: 1954-64, 1965-1977 and 1978 to the present, do not so neatly characterize the evolution of provincial activity. During all three periods, the provinces have regulated land use and provided sewers, water supplies and roads, all of which directly affect the location, type and price of housing. In almost all provinces these responsibilities have been delegated to municipalities. The federal government provided loans and grants for the construction of water and sewage treatment facilities until the cancellation of the Community Services Contribution Program in 1981.

Aside from land use regulation and servicing, the provinces played little role in housing policy during the 1954-64 period.[1] They had few independent programs and were followers rather than initiators in joint federal-provincial undertakings under the National Housing Act. There were several reasons for the federal dominance. During the war the central government had been involved in the construction of housing for workers in the armaments factories and after the war in the construction of housing for the returning veterans. Both meant a substantial involvement in housing matters, direct federal-municipal negotiations and a momentum which carried on until the early 1960's. The provinces did not object; partly because their governments lacked the administrative and technical skills to undertake independent activity. Perhaps most important of all, the principal policy problem of the time was to develop the mortgage market, an area of clear federal responsibility. Provincial activities were mainly contributing 25 per cent of the capital cost and 25 per cent of the operating subsidy in a partnership with the federal government under the federal-provincial (public housing) program. Table 2-1 of the previous chapter shows this remained a rather small program. Several provinces did not participate in the early years. The provincial financial commitments perhaps even overstate their involvement because, although local initiative was required before a federal-provincial public housing project could be started in any community, Central Mortgage and Housing Corporation was the true driving force involved 'every step of the way, from the original municipal-provincial request to the ultimate appointment of a local housing authority to administer and manage the completed dwelling' (Rose, 1980, 34).

This began to change in the early 1960's leading to new arrangements under the 1964 amendments to the National Housing Act. The provinces, having overseen a decade of rapid urban growth and urbanization, had begun to develop expertise in housing matters. There was a public desire to increase the amount of public housing provided, but the partnership arrangement did not seem a workable approach. And further, the provinces wished to assert their constitutional responsibilities and had grown resentful of direct federal-municipal dealings. The 1964 amendments offered new assistance terms for public housing. The federal government would offer loans for 90 per cent of construction costs and grants for 50 per cent of the operating losses to provincial or municipal public housing agencies. The federal government was no longer a partner, becoming only a financial contributor. These and other amendments to the terms of the limited divided housing and urban renewal programs meant that responsibility for housing assistance was 'put squarely in the laps of the provincial governments' (Rose, 1980, 41).

In order to exploit the new NHA terms, provincial governments created special agencies. The first to be created was the Ontario Housing Corporation in 1964, which immediately embarked on an ambitious public housing program. In 1967 the Alberta Housing and Urban Renewal Corporation, the Quebec Housing Corporation, the Manitoba Housing and Renewal Corporation were begun and the duties of the Nova Scotia Housing Commission were extended to permit usage of the new terms. By 1968, all but two provinces had established their own administrative instruments. The British Columbia Housing Management Commission was operational in 1970 and the Saskatchewan Housing Corporation in 1973. In the late 1960's, these housing agencies were mainly involved in the public housing program with the federal government and had few independent programs. Tables 3-1 and 3-2 show the level of federal lending under the public housing program by province; provincial lending would be about 10 per cent of this figure.

The establishment of these agencies was especially important because a body of administrative and technical skills was developed which would permit the launching of independent provincial programs. These emerged mainly through the 1970's. The first, in 1967, were the Home Ownership Made Easy Plan (Ontario) and the Provincial Home Acquisition Program (British Columbia). The former involved the provision of low-priced building lots for lease and the latter assisted buyers of their first home with their down payments.

As the provinces embarked on their own, it becomes more difficult to summarize their activity. Four provinces are examined in more detail in subsequent sections of this chapter. All provinces utilized federal programs and augmented them with independent provincial programs especially suited to local needs and priorities. Sometimes provinces would utilize federal programs and mount parallel provincial programs to increase the level of assistance or to facilitate the combining of several federal programs or to help private groups use federal funds. At other times, a province would establish a full range of provincial programs, operating independently of the federal government.

The same instruments used by the federal government have been used by the provinces in their housing programs with the exception of mortgage insurance. The provincial programs have involved direct lending, either as first or second mortgages, to finance the purchase of existing houses or the construction of new housing. The mortgages were often at a lower interest rate, and had a longer term and amortization period and higher loan to value ratio than a conventional mortgage loan. There have been grants to subsidize housing expenditures by both owners and renters often operating as a deduction of a portion of property taxes paid from taxable personal income. There have been mortgage loans and grants to finance renovation of older housing. A uniquely provincial instrument,[2] rent controls, was used in all jurisdictions during national wage and profits controls and remains in some provinces.

The rationale for almost all provincial programs has been to provide housing assistance to specific groups. With the possible exception of in Alberta, there has not been a sense that all housing construction or all housing consumption ought to be subsidized or that the private flow of mortgage finance was inadequate or that private markets were restricting the supply of new construction. The emphasis has been on assisting low and medium income households with the purchase of a house, especially those households who are buying their first house. An exception is Quebec which has not promoted home ownership to the same extent (C.C.S.D., 1980). All provinces also have programs to increase the housing consumption of low income renters and owners through loans often secured by a mortgage and grants for the renovation of old, usually substandard, housing. Most provinces also have special programs lending to households and builders in small communities and rural areas (C.C.S.D., 1980).

The most comprehensive documentation of provincial housing programs was prepared for a study of "Future Fiscal Arrangements for Housing in Canada". A statistical addendum (Alberta, 1981) described housing activity from 1971 to 1981 in each of the provinces, dividing activity into pure federal, federal/provincial, and pure provincial categories. However even this study was filled with caveats (see Alberta (1981) for details) and concluded the section on data sources with the following statement. "As a result of these limitations readers should be very cautious in using the updated tables for inter-provincial comparisons. The information contained herein goes only part way in providing a consistent and comprehensive housing activity data base by province." Nevertheless, this is by far the best source available and permits the broad patterns of provincial housing activity since 1971 to be sketched with some confidence.

The statistical addendum reported the number of dwelling units (and hostel beds) which had been assisted under federal progams, federal/provincial programs and purely provincial programs. The data are summarized in Table 3-3 (data were not available for Quebec and Nova Scotia). The federal and federal/provincial programs were described and discussed in the previous chapter and are pooled together in Table 3-3. It should be remembered that the level of assistance per assisted dwelling unit varies greatly under the various programs and that the number of assisted dwelling units does not measure the net additions to total housing starts as a result of government housing programs. Table 3-3 shows the pattern of federal activity already discussed: a high level of involvement until 1977, and then sharp contraction from

1978 to 1981. In 1977, almost 40 per cent of all housing starts were federally assisted, but by 1981 this had fallen to 11 per cent. Provincial housing involvement does not follow the same pattern. It was high in the mid-seventies then was sharply cut back but then expanded dramatically in 1980 and 1981. Thus overall government activity peaked in 1977 without falling off significantly thereafter. It seems, very roughly, that the provinces cut back when federal involvement was large in 1976 and 1977, and then expanded to counteract federal restraint in 1980 and 1981.

The summary table, however, masks substantial variation among provinces. Table 3-4 reports the percentage of starts in each province which were assisted under purely provincial programs. On average over the period, Alberta and Saskatchewan had substantial independent provincial programs, Ontario, New Brunswick and P.E.I. had moderate involvement while British Columbia, Manitoba, Quebec, Nova Scotia and Newfoundland had few independent programs.[3] The trends over time also show substantial variation. Alberta, Quebec, New Brunswick and Nova Scotia have been increasing their purely provincial involvement while Saskatchewan, Ontario (with the exception of 1981) and Prince Edward Island have been cutting back.[4]

The provinces thus remain significantly involved in housing policy and in mortgage markets. Emphasis is on lending for middle income homeownership programs, housing renovation and to special groups such as the elderly, handicapped and those in small communities and rural areas. They continue to undertake the direct building of rental housing with federal government financial assistance under the federal-provincial and new non-profit programs. However, because the transition to the new non-profit terms is so recent and because high real mortgage interest rates have restrained public construction, it is still too early to tell how significant this joint activity will be over the next decade. The federal government has withdrawn as a source of funds to provincial and municipal non-profit agencies and so provincial mortgage lending may be expanded.

This broad overview of provincial housing activity is next supplemented by a more detailed look at the housing programs of Nova Scotia, Quebec, Ontario and Alberta.[5] For each province, a brief summary of housing activities over the last thirty years is followed by a description of current mortgage lending programs which do not involve the federal government. The description highlights the goals of the programs and the mechanisms of assistance. Of course, just as at the federal level, this is far from a complete picture of housing programs or even lending programs related to housing. Provinces have numerous other programs: some providing technical assistance to groups and municipalities regarding land use planning, building and development matters; others providing loans to municipalities for sewage and water treatment plants, neighbourhood facilities and downtown renewal; there are grants to defray housing costs for first-time home buyers, senior citizens and other special groups; some provide additional assistance to recipients of federal subsidies; the list goes on and on. The emphasis here is on mortgage lending under independent provincial programs.

Alberta[6]

The Alberta Government became significantly involved in housing with the establishment of the Alberta Housing and Urban Renewal Corporation in May of 1967. This crown corporation renamed simply Alberta Housing Corporation (AHC) in 1970, was charged with facilitating the provision of appropriate housing accommodation at reasonable cost for low and moderate income families, senior citizens, students and other groups across the province. AHC was permitted to build or buy housing for rental or sale; assemble and develop land; administer its own housing developments; redevelop substandard areas; provide mortgages and undertake studies. It obviously was to involve itself in all aspects of housing policy.

Entering into the 1970's, AHC operated public, senior citizen, student and northern housing assistance programs as joint endeavours with the federal government. In 1972, the province stepped up its land banking, using federal funds and following the 1972-73 ammendments to the NHA, was the first province to administer the Neighbourhood Improvement Program.

In the 1970's Alberta moved beyond joint endeavours to mount major programs independently. These assistance programs involved large amounts of mortgage lending, outlined in Table 3-5, and often annual subsidies. At first, AHC made direct loans to homeowners for the construction of new homes, purchase of existing homes or home improvements and later extended the lending to finance mobile home parks and construction of rental housing. The clear emphasis was always on encouraging and assisting households to become homeowners. Alberta's activities then increased dramatically in the middle of the decade and continue to grow. A Ministry of Housing and Public Works was created for program development and supervision, and the Alberta Home Mortgage Corporation (AHMC) was established to handle Alberta's growing mortgage lending. Lending more than doubled to $131 million from 1975 to 1976. Four new programs were established, which are described in more detail below. The Starter Home Ownership Program (later joined with the Direct Lending Program to be called the Family Home Purchase Program) and the Farm Home Lending Program offered mortgage loans and subsidies depending on the applicant's income and house payment. The Core Housing Incentive and Modest Apartment Programs provided high ratio mortgage loans to finance the construction of modest rental buildings. Under the former, the interest rates were below market levels and in return builders agreed to controlled rents on one half the units in a building. In both the ownership and rental areas, Alberta not only provided mortgage financing but also ongoing subsidies which reduced the price of housing for program participants.

The restraint seen in recent years in some provinces and at the federal level is not evident in Alberta, except insofar as federal restraint has reduced joint endeavours. Lending continues to grow and recently new programs have been added extending the home ownership assistance to finance mobile home purchases and the construction of housing which is finished on the outside and habitable but not completely finished on the inside. New rental programs offering mortgages and special tax advantages and programs for rural and remote housing have also been mounted. AHMC also will finance projects under the new NHA Non-Profit Program (CMHC suggests that non-profit groups obtain private sector financing).

As the descriptions of these various programs below make obvious, Alberta has its own initiative in almost every area normally occupied by governments in dealing with housing. It has established a separate housing assistance system involving considerable mortgage lending. Only home repair and renovation programs are missing from the list and that is only because this was handled through grants rather than mortgage loans.

The Alberta Family Home Purchase Program, formerly the Starter Home Ownership Program, is designed to stimulate construction of modest housing and to enable low and moderate income families to buy new or existing housing. AHMC provides loans of up to 95 per cent of the lending value of the house and land up to $53,200 plus the mortgage insurance fee for existing homes; and 95 per cent of the lending value up to $63,360 plus the mortgage insurance fee for new housing. The loans are at AHMC's conventional interest rate which is near the market rate. Subsidies, depending on the applicant's income and house payments, start at an income of $25,000 and increase as income decreases to a maximum subsidy of $3,240 per year ($270 per month). The need for the subsidy is reviewed every 30 months. An additional subsidy of $20 per month for a period of 30 months is available to first-time homeowners who meet program guidelines and who purchase new homes complying with special size limits.

The Farm Home Lending Program provides financial assistance to farmers for the construction of new homes or for the purchase of existing homes to be relocated on a farm for use by the applicant's household or by farm helpers and their families. AHMC provides a mortgage at its near-market interest rate and subsidies are provided depending on adjusted gross income and amount of house payment, up to $2,208 per year. Maximum loan amounts are $42,000 and loan amortization periods are up to 40 years.

The Mobile Home Lending Program provides mortgages to low and moderate income families for the purchase of mobile homes and to builders and dealers who wish to acquire and place new units on permanent foundations on lots for sale to qualified purchasers. Loans and subsidies are provided as under the Alberta Family Home Purchase Program or Farm Home Lending Program, depending on the program for which the applicant qualifies.

The Co-operative Housing Action Program assists low and moderate income families who are willing and able to construct part or all of a house. Assistance is provided in the form of advice, training and financial aid. Advice is given to the applicant about the formation of a buying co-operative to achieve savings in purchasing materials, on the formation of building groups and about the development of a construction work plan. Training is offered to the co-ops concerning parts of the construction process which they can handle. Loans and subsidies are provided under the Alberta Family Home Purchase Program.

The Shell Housing Program facilitates the construction for ownership by low and moderate income families of shell housing - housing which is completely finished on the outside, and while habitable is not completely finished on the inside. Loans and subsidies are provided as under the Alberta Family Home Purchase Program or the Farm Home Lending Program. The loan amount will be based on the value of the shell house, as opposed to the completed structure. Mortgage funds will normally be completely advanced when the shell home is finished.

The Core Housing Incentive Program is designed to stimulate the construction of low rental accommodation, particularly modest amenity accommodation in major urban areas. Loans to builders of up to 95 per cent of the appraised cost of land and buildings, as determined by AHMC, at below market interest rates are available. The amortization period is 50 years and the term is 15 years.

Rents for 50 per cent of the units must fully reflect the benefits of the special financing and the units must be rented to moderate income households.

The Modest Apartment Program was devised to stimulate the construction of small rental housing projects in smaller centres in order to provide rental housing for moderate income families and individuals living in these areas. AHMC provides loans of up to 90 per cent of the value of the land and buildings. The loan carries an interest rate near the market rate and is amortized over a period up to 40 years.

The Senior Citizen Lodge Program finances retirement accommodation with a substantial degree of home-care services and affordable rents. Mortgages are available for 100 per cent of the construction cost of new lodges, including all furnishings and fixtures and for the cost of upgrading or increasing the size of existing lodges. Municipalities assume responsibility through Senior Citizens Foundations for the projects upon completion. Rents, which in 1979 were $168.33 per month per person for double occupancy and $190.33 per month for single occupancy, do not cover costs. Operating losses are paid by the municipality. However, if losses exceed an amount equal to revenues from a two mill tax rate, the province will provide financial assistance equal to 50 per cent of the amount above the two mill rate under the Lodge Assistance Program.

The Nursing Home Financing Program provides mortgages to voluntary non-profit organizations for the construction of nursing homes. AHMC provides loans at the NHA interest rate for up to 95 per cent of construction costs to a current maximum of $27,000 per bed. The amortization period is up to 40 years and the term will be five years.

The Starter Home Ownership Program was intended to assist lower income families in the purchase of their first homes and to stimulate the construction of low priced modest homes. Mortgages at conventional interest rates were provided to applicants. Interest rate subsidies were then applied, scaled to income. Incomes were reviewed every 2½ years to re-evaluate the interest assistance required. This and the following program became the Alberta Family Home Purchase Program.

The Direct Lending Program provided mortgage loans to low and medium income families where demand was not being met by other mortgage lenders. AHMC made available a 95 per cent loan. Sweat equity could be used as a portion of the required down payment and/or a reduction of the amount of the mortgage on the home. A reduced interest rate loan was available to applicants with a gross debt service of at least 28 per cent. Interest rates ranged from 9½ per cent for an adjusted family income of $10,000 or less, to 10¼ per cent for an adjusted family income of up to $16,500. Loans were also available to finance rental accommodation.

Ontario[7]

The Government of Ontario first became involved in housing policy in 1946 with the enactment of the Planning and Development Act. However, this legislation facilitated municipal-federal arrangements and did not involve direct provincial activity. With the passing of the Housing Development Act in 1948, the province provided assistance to municipalities involved in federal-municipal projects. Low cost second mortgages for individuals purchasing homes under the NHA were also offered. Over 15,000 homeowners benefited from these cheap second mortgages between 1948 and the termination of the program in 1950. Provincial activity was then confined to participation in joint federal-provincial endeavours such as federal-provincial public housing.

Ontario's activities increased after 1964 with the establishment of the Ontario Housing Corporation (OHC) following the NHA amendments. Through OHC and using federal and provincial financing, a large number of public housing units were constructed. In 1970, almost 20 per cent of all housing starts in Ontario were for public housing. An experimental program of acquiring existing housing for public rental was initiated. This program, however, was cancelled in 1967 due to its inability to produce a high volume of units.

Provincial housing activities then expanded continuously until the late 1970's. Ontario participated in joint federal-provincial programs, offered supplemental assistance to federal programs and mounted programs independently. The Housing Corporation Limited was established to make provincial mortgage loans. The Home Ownership Made Easy Plan (HOME), begun in 1967, was the major independent initiative. The extent of activity under HOME is presented in Table 3-6. The Plan provided lots for lease, which the province had assembled and serviced, with the lease based on the book value rather than the market value of the land. Houses built on the land could not sell above a maximum price. Other smaller programs offered mortgages for houses and condominiums built according to the HOME Plan guidelines.

In 1972, a Task Force on Housing Policy was commissioned to review housing policy in Ontario in light of the 1972-73 amendments to the NHA. The Task Force recommended the creation of a Ministry of Housing which would oversee the operations of OHC's assistance programs. It also recommended the extension of land assembly programs; more programs to increase the supply of serviced residential land; greater involvement of municipal governments in housing policy and greater assistance to groups with special needs. The Task Force also emphasized that the private market should assume the main responsibility for meeting housing needs.

In response, Ontario's independent housing activities increased dramatically. A Ministry of Housing was created and the Ontario Mortgage Corporation was established, taking over from the Housing

Corporation Limited, to handle the increased mortgage lending. The Ontario Housing Action Program, a large umbrella for numerous activities to stimulate housing construction in high growth areas, was initiated in 1973. There were loans to municipalities for sewer and water facilities, grants to offset property tax increases resulting from new housing developments, mortgage loans for builders of housing which followed the HOME plan guidelines, technical assistance to speed planning and approvals and attempts to streamline the entire process of land use regulation.

The recommendations for increased municipal responsibility called for by the Task Force were implemented by the Ministry. Such responsibility included the preparation by municipalities of housing policy statements concerning production targets and funding levels, to be submitted to the Ministry. Local housing corporations were formed throughout the province to administer public housing and municipalities began their own land banking schemes. The City of Toronto was one of the first cities to introduce a non-profit corporation. In the following year the City of Toronto established a Department of Housing. Local governments however never had lending or assistance programs of their own, confining their activities to zoning and servicing land and facilitating the use of the programs of upper levels of government.

Around this time many other programs were begun. The Community Integrated Housing and Accelerated Family Rental Housing programs offered mortgages at attractive rates if owners would agree to controls on rents and would permit tenants assisted under the federal-provincial Rent Supplement Program to occupy up to 25 per cent of the units. The province began to offer mortgages at attractive rates to participants in the HOME Plan and the Preferred Lending and Condominium Housing Programs made attractive mortgage loans for houses built following HOME Plan guidelines. The Ontario Home Renewal Program made per capita grants to municipalities for use as loans and grants to homeowners who would renovate their houses in areas not covered by the federal Residential Rehabilitation Assistance Program.

Large amounts of money were lent. Table 3-7 shows the mortgage assets of the Ontario Government's agencies as a result of lending under these independent programs. From 1972 to 1977, over $700 million in provincial mortgage funds were advanced. However, even more quickly than it had begun, Ontario's lending was cut back. In 1978-1979, no new mortgage commitments were made. As well, provincial assistance which supplemented federal programs was curtailed as federal activities wound down.

Below, further details are provided of Ontario's housing programs involving mortgage lending which operated independently of federal programs.

The Home Ownership Made Easy Plan aimed to facilitate home ownership among moderate income groups by providing building lots which could be leased for their book value. The program was altered on several occasions before it was completely terminated in 1978. The original plan, implemented in 1967, provided for the leasing of lots for up to 50 years with lease payments based on what the government paid to acquire and service the land. This had the effect of reducing the downpayment since the purchase of the land was unnecessary and reducing the carrying costs because of the attractive lease terms. The purchaser also had the option of buying the lot after five years at the market price when the lease began. Homes built on HOME lots had to be 'no-frills' housing priced below a given maximum.

In 1973, the terms under which the leaseholder could purchase the lot after the initial five-year period were changed so that the purchase price was based on current rather than initial market value. Also, first mortgages from the Ontario Mortgage Corporation were made available to finance the purchase of the house. In 1975, the land lease system was converted into a second mortgage system. Principal and interest payments on the mortgage were based on the book value of the land and NHA interest rates, a five-year term, with 35-year amortization. The difference between book and initial market value of the land and was repayable either on sale of the property or the termination of the 35-year mortgage.

In March 1977, assistance under HOME was changed to a provincial grant to be added on to the Federal AHOP. The HOME program was terminated in June 1978, when AHOP was scaled down to a graduated payment mortgage.

The Condominium Housing Program was intended to facilitate homeownership for low and moderate income families. Begun in 1967, the program provided land and/or mortgage financing to builders and developers who would produce condominiums within the price and buyer qualification guidelines of the HOME Plan. The mortgages were for up to 95 per cent of the building value and at below market interest rates. Applicants had to fulfill certain eligibility criteria; for example in 1975 the combined incomes of members of the household could not exceed $17,000. There were also controls on resale prices for the first five years.

The Preferred Lending Program like the previous program facilitated home ownership for moderate income families by providing builders and developers, who sold houses within the basic guidelines of the HOME plan, with mortgage financing at below market interest rates. Beginning in 1973 and depending upon the availability of funds, the Ontario Mortgage Corporation provided up to 95 per cent financing at interest rates that were generally 1.5 per cent to 2 per cent below market rates.

The Ontario Housing Action Program was a package of initiatives designed to increase housing construction in high growth areas and to encourage private developers to build more units for families of low and moderate incomes. For homes priced according to the

HOME Plan guidelines, the Ontario Mortgage Corporation provided 95 per cent mortgages at below market rates. Mortgages, at less subsidized but still attractive rates, were also available for homes slightly outside the guidelines. Purchasers of units built before March 31, 1976 were eligible for mortgage interest subsidies to keep rates below 10¼ per cent. OHAP also provided interest free loans for construction of major services and storm sewers, grants to municipalities to offset property tax increases following new developments, and a staff to coordinate and speed the approval process. The program began in 1973 and was terminated at the end of 1976.

The Accelerated Family Rental Housing Program was designed to increase the supply of rental units for low and moderate income earners. A mortgage loan for up to 95 per cent of costs was available at an attractive interest rate. Up to 25 per cent of the units in each new building had to be under a rent supplement arrangement lasting for a period of 15 years. The program was started in November 1974. Operating losses were financed on a 50:42 ½:7½ federal-provincial-municipal basis.

The Community Integrated Housing Program, like the previous program, sought to expand the rental housing stock and ensure an adequate supply of housing for lower income families. The Ontario Mortgage Corproation provided second mortgage financing to 95 per cent of the building value (the loan could only be 35 per cent of value) in return for the owner making up to one quarter of the units available to the Rent Supplement Program.

The Ontario Home Renewal Program is intended to preserve and improve the existing housing stock in Ontario by providing financial assistance to owner-occupants. Annual per capita grants are made to municipalities who in turn provide loans to owner-occupants enabling them to bring their dwellings into compliance with maintenance and occupancy standards. The maximum loan available is $7,500, of which $4,000 may be forgiven if the applicant earns $6,000 or less annually. The interest rate on the loan ranges from 8 per cent, for people earning $8,000 or more annually, to nothing, for people earning $3,000 or less. In order to receive the grant portion of the OHRP loan, the recipient must occupy his dwelling for a determined period of time. Municipalities of 10,000 persons or less, excluding regional municipalities, are eligible for additional grants of $25,000. The program was designed to provide the benefits offered under the Residential Rehabilitation Assistance Program to owner-occupants in communities outside RRAP designated areas. Since 1976, loans have been available to the landlords for renovations of units rented by low and moderate income households.

Quebec[8]

The Quebec Government's involvement in the housing sphere began to expand when the Quebec Housing Corporation Act was passed in

1967 which established the Quebec Housing Corporation (QHC). QHC became directly responsible for facilitating and encouraging the physical improvement of Quebec urban communities, facilitating home ownership, ensuring reasonable rents and administering the Family Housing Act. At the request and with the co-operation of the municipalities, QHC prepares and makes programs operational. After housing projects are completed, QHC passes administrative responsibility for the project to the local Municipal Housing Bureau.

Entering the 1970's, QHC provided assistance in two major areas: urban renewal and public housing for senior citizens and for families. In 1973, sixteen urban renewal projects were approved involving just over $11 million in grants and loans. Almost all lending for housing was a joint federal-provincial endeavour.

Declining assistance to low income groups and QHC's inability to keep pace with Ontario's participation in housing assistance, led to a review of housing policy in Quebec. The Task Force on Quebec Housing Policy concluded in its Report on Housing Policy in Quebec 1976, that new programs were required to stimulate activity in the areas of ownership, rental, restoration-improvement and land servicing. In response to this report, QHC adopted a new approach towards its housing assistance and concentrated on increasing the number of co-operatives and other non-profit housing operations in order to stabilize rents for low and moderate income families. The use of joint federal-provincial programs continued however, and Quebec mounted almost no independent programs. In 1979, Quebec had a lower value of loans outstanding related to housing than any other province (E.C.C., 1981).

The Construction of Low Rental Housing Program is designed to make available low rental housing units for low and modest income individuals or families. The Quebec Housing Corporation carries out the program and remains the owner but turns over the operation and the administration to non-profit agencies or to municipal housing boards.

The Construction of Hostels Program makes mortgage loans for the construction, acquisition or improvement of low rental housing of the hostel type which provides accommodation for senior citizens, needy children or to any other group designated as underprivileged. QHC provides 100 per cent financing of recognized costs with terms of up to 50 years and at a preferential interest rate.

Nova Scotia[9]

The government of Nova Scotia was more involved in housing than most provinces in the pre-war and early post-war years. The first housing assistance in Nova Scotia was directed towards co-operatives, in particular building co-operatives of households who would construct their own houses, and this has remained a feature of provincial housing policy. The first co-operative projects were financed by the Nova Scotia Housing Commission (NSHC) created in 1932. From 1936 to 1953, co-operative housing was handled independently by the province. However, in 1953 the Housing Commission was authorized to enter into federal-provincial cost-sharing arrangements regarding housing. As a result, housing programs expanded to include joint federal-provincial operations producing public housing for families and senior citizens. Co-operative housing received 75 per cent of its mortgage financing from the federal government while the Housing Commission provided the remaining 25 per cent. The administrative responsibility rested with the province.

Public housing and co-operative housing dominated the Housing Commission's attention until the late 1960's. In 1967, with the passing of the Housing Development Act, new responsibilities were assigned to the Housing Commission. It became involved in land development, land banking and mobile homes. The Housing Commission was to study housing needs; make recommendations for the improvement of housing conditions and encourage and provide public and private initiative in housing and neighbourhood improvement matters. It became the vehicle for coordinating provincial participation in federal-provincial programs.

Much of the assistance provided by the Commission was developed under partnership agreements with CMHC. In this way, the programs under the National Housing Act were tailored to fit the preferences of Nova Scotia. Usually the mortgages loans were made up of a 75 per cent federal and 25 per cent provincial contribution and the loans were just below market rates. Under the Co-operative Housing Program, NSHC began to subsidize mortgage payments in 1971. The federal AHOP was converted to a co-operative program under an agreement with CMHC, and later Nova Scotia added further subsidies of its own in addition to the federal.

In the late 1970's, Nova Scotia began to mount programs independently. One program offered mortgages to finance the conversion of larger homes into apartments. The Self-Help Housing Program supplied low interest mortgage loans to households building their own home. These complemented an earlier grant to buyers of a newly constructed home and a program which offered additional subsidies so households with relatively modest incomes could participate in AHOP. Nova Scotia also had its own renovation programs. The Senior Citizens Assistance Program and the Small Loans Assistance Program provided subsidies and mortgage loans for the rehabilitation of single family homes. Together these reflected a clear preference for ownership as the form of housing tenure in Nova Scotia housing policies (C.C.S.D., 1980, 15). Lending under these initiatives is outlined in Table 3-8. Clearly, Nova Scotia's independent programs have not been restrained in recent years; indeed they have just begun.

In sum, the principal housing programs in Nova Scotia have been federal-provincial undertakings modified to provincial priorities.

The province occasionally offers additional assistance under these and emphasized cooperative housing. Nova Scotia has now begun to mount a few independent programs. Those programs which involve mortgage lending are described in more detail below.

The Small Loans Assistance Program provides low interest loans to low and moderate income households for repair, alterations or additions to single family homes and for the completion or partial completion of a single family home. Loans are available to a maximum of $10,000 at a favourable interest rate. Loans are secured by a first mortgage or second mortgage on the house. Where a second mortgage is taken, the balance owing on the first mortgage shall not exceed 50 per cent of the appraised value of the dwelling. If the dwelling is sold, the balance of the loan becomes payable.

The Senior Citizens' Assistance Program is designed to help senior citizens wishing to remain in their own homes, but who cannot afford to carry out the repairs which would extend their residency. The program provides grants up to a maximum of $2,500 representing 75 per cent of the costs of labour and materials. The applicant is responsible for paying the remaining 25 per cent. If the applicant is unable to afford the 25 per cent portion, low interest loans may be made available under the Small Loans Assistance Program.

The Apartment Conversion Program is intended to increase the stock of apartment accommodation by converting the unused portions of larger homes into apartments. Loans of $5,000 per new apartment created are available up to a maximum of $20,000 for four units. Loans are amortized over a 10-year period and are secured by a first or second mortgage on the property, the combined value of which must not exceed the appraised value of the property. The mortgages are at interest rates well below market levels. The balance of the loan becomes due upon sale of the property.

The Housing Emergency Repair Program was one of Nova Scotia's first independent initiatives. Begun in 1977, it provided forgiveable loans for the repair of single family units. Then in the following year it was converted into a pure grant program. Since such a significant portion of those assisted were senior citizens, it was decided to restructure programs to deliver assistance more directly. The previous three programs emerged as a result.

The Self-Help Housing Program provides funds for the construction or renovation of modest housing for low and middle income families. The program provides low interest, high ratio mortgages, plus an education program to assist the participants in learning the necessary aspects of house construction. Applicants must have a combined family income of less than $30,000.

The New Home Mortgage Program was recently begun to relieve the burden of high interest rates and stimulate the construction of single family homes. NSHC offers high-ratio, low interest mortgages to low and moderate income families. The interest rate varies with income from a low of 11 per cent for those with incomes of less than $23,000 to a high of 15 per cent for those with incomes of $30,000.

Table 3-1

Loans for Public Housing Projects, New and Existing Housing, By Province
1964-1970
($000)

Province	1964	1965	1966	1967	1968	1969	1970
Newfoundland	-	-	-	2,851	-	1,159	267
P.E.I.	-	-	-	-	-	-	-
Nova Scotia	-	-	-	615	2,154	531	341
New Brunswick	-	-	-	-	3,788	5,588	7,796
Quebec	-	-	-	-	5,634	59,522	65,628
Ontario	261	15,471	42,881	104,198	87,472	122,870	128,438
Manitoba	-	-	-	-	-	1,020	10,902
Saskatchewan	-	-	-	-	293	-	-
Alberta	-	-	-	-	-	4,900	11,774
British Columbia	-	-	-	-	-	-	-
N.W.T.	-	-	-	-	-	-	-
Yukon	-	-	-	-	-	-	-

Source CMHC (various years).

Table 3-2

Loans for Public Housing Projects, New and Existing Housing, By Province
1971-1977
($000)

Province	1971	1972	1973	1974	1975	1976	1977
Newfoundland	2,088	636	1,598	4,434	5,337	11,013	3,871
P.E.I.	99	705	762	3,914	-	-	-
Nova Scotia	3,551	8,017	5,427	3,988	3,834	1,059	1,496
New Brunswick	6,066	1,638	4,799	5,967	4,685	4,846	853
Quebec	53,872	62,323	4,010	863	13,836	25,519	27,905
Ontario	152,736	113,681	105,341	82,174	104,555	116,720	49,513
Manitoba	43,915	31,643	6,985	14,293	30,449	48,207	22,400
Saskatchewan	-	-	-	-	-	-	-
Alberta	11,958	7,890	9,413	7,846	29,347	30,825	19,103
British Columbia	-	-	-	19,141	35,307	2,881	-
N.W.T.	-	1,243	865	1,010	10,117	11,627	8,770
Yukon	-	-	1,012	-	1,211	511	-

Source CMHC (various years).

Table 3-3

Assisted Starts as a Percentage of Total Starts[1]
1973-1981

	1973	1974	1975	1976	1977	1978	1979	1980	1981
Federal and Federal/ Provincial Programs	23	17	27	26	39	21	14	18	11
Provincial Programs	6	9	12	6	5	3	4	17	26
All Government	29	26	39	32	44	24	18	35	37

1 Excluding Quebec and Nova Scotia in all years and excluding Ontario in 1973.

Source Alberta (1981) and CMHC (various years).

Table 3-4

Provincially Assisted Starts as a Percentage of
Housing Starts in that Province
1971-1981

Province	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	Average
British Columbia	0	0	0	0	0	0	0	0	0	14	2	2
Alberta	2	4	9	13	15	18	16	10	15	47	47	21
Saskatchewan	n.a.	n.a.	46	25	25	15	8	5	2	5	11	16
Manitoba	0	0	0	0	0	0	0	0	0	0	0	0
Ontario	n.a.	n.a.	n.a.	11	16	4	1	0	0	0	34	8
Quebec	n.a.											
New Brunswick	1	3	2	3	5	5	5	7	8	17	19	8
Nova Scotia	n.a.											
Prince Edward Island	n.a.	n.a.	20	8	0	10	17	13	11	7	5	10
Newfoundland	n.a.	n.a.	5	7	0	0	0	0	1	4	13	3
All Canada[1]			6	9	12	6	5	3	4	17	26	10

[1] Excluding Quebec and Nova Scotia in all years, and Ontario in 1971, 1972 and 1973.

Source Alberta (1981) and CMHC (various years).

Table 3-5

Government of Alberta Mortgage Lending
1972-1980
($000)

Program	1972[1]	1973[1]	1975[2]	1976[3]	1977[3]	1978[3]	1979[3]	1980[3]
Direct Lending	10,316	34,433	62,228	64,449	57,680	46,729	80,574	190,414
Starter Home Ownership				22,112	30,639	18,732	36,942	
Farm Home Lending				169	385	118	121	589
Core Housing Incentive				35,922	57,985	52,721	30,905	76,411
Modest Apartment				8,464	7,461	22,787	13,641	5,344
Non-Profit (NHA)								8,999
Mobile Home				1,512	3,098	2,288	1,481	-
Total	10,316	36,433	62,228	131,113	157,248	143,375	163,664	281,168

[1] As of December 31.
[2] For the 15 month period ending March 31, 1975.
[3] As of March 31.

Source Alberta (various years a), Alberta (various years b).

Table 3-6

Activity Under the HOME Plan
1967-1976

Year	Number of Lots Disposed
1967	603
1968	2,197
1969	1,445
1970	936
1971	2,731
1972	3,785
1973	1,650
1974	3,910
1975	3,297
1976	3,952
Total	24,516

Source Fallis (1980).

Table 3-7

Mortgage Assets From Ontario Housing Programs
1970-1978
($ millions)

	Mortgage Assets of Housing Corporation Limited			Mortgage Assets of Ontario Mortgage Corporation[4]				
	1970[1]	1971[1]	1972[1]	1973[2]	1974[2]	1975[2]	1976[2]	1978[1,3]
HOME Plan	0.9	62.0	152.0	230.0	242.0	319.6	401.3	420.5
Preferred Lending					1.6	3.7	24.0	32.0
Community Integrated Housing					0.4	5.9	7.4	5.5
Ontario Housing Action Program						21.4	179.5	178.0
Accelerated Family Rental Housing							65.1	90.2

[1] As of March 31.
[2] As of December 31.
[3] No new commitments made from March 31, 1978 to March 31, 1979.
[4] Ontario Mortgage Corporation took over the mortgage portfolio of Housing Corporation Limited in 1974.

Source Ontario (various years a), Ontario (various years b).

Table 3-8

Provincial Government Mortgage Lending in Nova Scotia
1976/77 - 1980/81
($000)

Program	1976/77	1977/78	1978/79	1979/80	1980/81
Provincial Housing Emergency Repair	-	2,994	(2,992)[1]	(163)[1]	(245)[1]
Senior Citizen Assistance	-	-	-	1,258	1,993
Small Loans Assistance	-	-	-	416	609
Apartment Conversion	-	-	-	93	129
Self-Help	-	-	-	343	1,653
Total	-	2,994		2,110	4,384

[1] The program was converted from loans to grants. The bracketed figures are grants.

Source Correspondence with Nova Scotia Housing Commission.

Chapter 3: Notes

1 The activities of municipalities are properly considered provincial because municipalities have only powers delegated by the provinces. In the immediate post-war period municipalities acted somewhat independently and dealt directly with CMHC in housing matters. Recently some cities have become active again in their own right. Toronto has established its own department of housing for example. Municipal initiatives are still, however, mainly confined to exploiting provincial or federal programs.

2 Provinces have the right to set controls on rent because of their responsibility for property and civil rights. Many provinces established controls only at the request of the federal government.

3 The characterizations of Quebec and Nova Scotia are based on expenditure data rather than numbers of assisted dwelling units (Alberta, 1981).

4 These data relate to units assisted and thus reflect new assistance in that year. Actual expenditures under housing programs may be rising each year, reflecting the payments which must be made under assistance schemes begun in previous years.

5 The previous provincial overview was updated just prior to publication of this discussion paper. It proved impossible to update the sections on the separate provinces. The original work was submitted to the Economic Council of Canada in 1981 and often available data were a few years out of date. These sections thus cover the period of the 1970's.

6 The overview and descriptions of Alberta housing programs are based on Alberta (various years a), (various years b) Alberta (1980), C.P.A.C. (1976), CMHC (1976b) and Rose (1980). In the text discussing Alberta's and other provinces' programs there are many quotes from government publications. To avoid numerous citations and make reading easier these quotations have not been indicated. The footnotes acknowledge the sources. The same was true for the sections on federal housing programs.

7 The overview and descriptions of Ontario housing programs are based on Fallis (1980), CMHC (1976b), Ontario (1980), (1977), (1976), (1975), (1974), (various years a), (various years b), O.W.C. (1973), and Rose (1980).

8 The overview and descriptions of Quebec programs are based on Quebec (1977), (1976), (1972-73), C.P.A.C. (1976), CMHC (1976b), and Rose (1980).

9 The overview and descriptions of Nova Scotia housing programs are based on C.C.S.D. (1980), Nova Scotia (1980), (various years), Roach (1974), C.P.A.C. (1976), MacNutt (1971), CMHC (1976b) and Rose (1980).

4 EVALUATION OF EXISTING PROGRAMS

Both federal and provincial governments are clearly very involved in Canadian mortgage markets. The federal government provides mortgage insurance and both levels make mortgage loans, often with terms, interest rates or subsidies to reduce the annual carrying costs. Despite cutbacks over the last few years, the level of involvement remains considerable. There is however debate in most provinces, at the federal level and indeed in most Western countries about what is the appropriate role for government. The purpose of this chapter, as part of that debate, is to assess the existing mortgage related programs of the federal and provincial governments by comparing them to the recommendations of neoclassical welfare economics about the optimal role of governments in mortgage markets. It draws together the work of the previous two chapters of this discussion paper and the work of a companion discussion paper - Governments and the Residential Mortgage Market I: A Normative Analysis (Fallis, 1983b). The companion paper applied the welfare economic rationale for government intervention to housing matters and suggested the optimal policy related to mortgage markets. Chapters 2 and 3 of this paper described the mortgage programs of the federal and provincial governments emphasizing their rationale or objectives and the instrument of intervention. In the following sections, the welfare economic rationale for government intervention will be compared with the stated objectives of housing programs; the optimal instruments recommended by economic theory will be compared with actual instruments; and the costs of non-optimal policies will be discussed.

Policy Objectives

In assessing any program it is important to establish whether a criticism is based on different values than the values of those who mounted a program. A program providing housing assistance may be criticized because one does not accept that housing is a merit good. This is a perfectly valid criticism and there can be debate among those holding different values - suggesting one side has not thought clearly through their values or that one side has not recognized the implications of their position. But social science cannot verify which value is right by an appeal to the facts. This section discusses whether differences between actual and optimal policies might be attributable to differences in values or objectives.

When stated in general terms, government economic objectives in Canadian society and the objectives assigned to government by welfare economics are very similar. Welfare economics speaks of the maximization of social welfare, which can be realized by a combination of private and public decisionmaking. Government decisions should deal with non-competitive behavior, uncertainty, externalities, merit goods, income distribution and stabilization of the economy to secure full employment, stable prices and economic growth. The actual role of government is very similar.

People speak of government working for a just society or representing the public interest or seeking 'the greatest good for the greatest number.' The terms of reference of the Economic Council of Canada refer to Canada's basic social and economic goals, described briefly as "full employment, a high rate of economic growth, reasonable stability of prices and an equitable distribution of rising incomes" (E.C.C., 1964). The Report of the Royal Commission on Taxation stated "four fundamental objectives on which the Canadian people agree are: (1) to maximize the current and future output of goods and services desired by Canadians; (2) to ensure that this flow of goods and services is distributed equitably among individuals and groups; (3) to protect the liberties and rights of individuals through the preservation of representative, responsible government and maintenance of the rule of law; and (4) to maintain and strengthen the Canadian federation" (Canada, 1966). Neither welfare economics nor Canadian society see private as opposed to collective decisionmaking as an end in itself, although if the choice systems produce the same outcome both usually favour private choice. Thus, the broad approach of welfare economics and of Canadian governments are alike, although the terminology used in describing each may be somewhat different.

In housing matters specifically, the similarity in broad objectives continues. Governments at all levels have asserted that adequate, affordable housing is a right of Canadians. The federal government "has adopted the basic principle that (says) it is a fundamental right of Canadians, regardless of their economic circumstances, to enjoy adequate shelter at reasonable cost" (Hansard, 1973). Indicative of the views of provinces, the Ministry of Housing in Ontario declared "that adequate housing at affordable prices is a basic right of all residents of Ontario" (Ontario, 1974). By implication, the objective of governments is to see that Canadians enjoy adequate, affordable housing.

In welfare economics, the right to adequate housing is represented through the concept of housing as a merit good or through donor preferences. However, the right to affordable housing does not appear to be part of the welfare economic approach, unless it is a proxy for other issues. Society may care about housing affordability, usually measured as the percentage of income spent on housing, because if too much is spent on housing then not enough income remains to be spent on other necessities like food and clothing. Housing affordability is therefore an issue only for low or moderate income people. If a wealthy household is confronted with rising real house prices and mortgage interest rates and spends 35 per cent of its income on housing, this would not be a social problem. Under this interpretation, the housing affordability concept can be seen as a proxy for concern about the consumption of several merit goods or about the distribution of income and therefore is consistent with the approach of welfare economics (see Fallis (1983a) for a more detailed discussion).

If, however, society believes that everyone has the right to acquire the housing they desire spending less than 25 or 30 per cent of their income, then working to insure such a right is not a role assigned government by welfare economics. Some appear to espouse the latter definition of affordability. But the more widely held view is the former because affordability is usually only considered a problem for lower and moderate income households. Therefore affordability can be analysed as concern about several merit goods or income distribution.

Thus, the fundamental values of welfare economics and Canadian political culture are not significantly different. This is hardly surprising as both reflect a liberal political philisophy. Any differences between observed and optimal policy do not result from different approaches to the fundamental role of government.

There may be one difference between the welfare economics of this monograph and Canadian political culture and that concerns home ownership. It may be that society values home ownership.1 A social value placed on home ownership can, of course, be analysed within welfare economics as a tenure externality or a merit good, but these have not been regarded as important. (Although even if they were, existing income tax subsidies are likely more than sufficient to deal with them).

However, as one seeks to identify the rationale for, or objectives of, specific housing policies by reading the statements of politicians, the enabling legislation and the publications of the agencies, ministries or departments responsible for mortgage interventions, this coincidence with the approach of welfare economics is much less evident. The purpose of the National Housing Act as stated in its preamble is "to promote the construction of new houses, the repair and modernization of existing houses, and the improvement of housing and living conditions." Chapters 2 and 3 have described the purposes of many federal and provincial programs, so a few citations will suffice here. The objective of NHA mortgage insurance "is to promote high volume and stability in the flow of non-governmental mortgage funds to residential mortgage financing for new and existing housing"; and of the Assisted Home Ownership Program "to encourage the production of moderately priced housing for homeowners, through the provision of interest reduction loans and subsidies to qualifying purchasers" (CMHC, 1976b). The purpose of the Ontario Home Renewal Program is "to assist owner-occupants to repair their houses, especially substandard structural and sanitary conditions, plumbing, heating and electrical systems and insulation" (Ontario, 1980). In Alberta, the objective of the Core Housing Incentive Program is "to stimulate the production of market rental housing and modest rental housing in all communities with a population over 5,000 and in specified growth communities" (Alberta, 1980). In Nova Scotia, the New Home Mortgage Program is intended "to relieve the burden of high interest rates for new home buyers in Nova Scotia and to stimulate the building industry by making funds available for the construction of single family dwellings" (Nova Scotia, 1980).

These published objectives of actual housing programs do not seem to reflect a rationale for government intervention like that of welfare economics.[2] They cannot easily be interpreted as concern for lack of competition or externalities or income distribution or economic stabilization. However, this is not because existing programs reflect a different approach but rather that the rationale for intervention and program objectives are not well articulated. Many of the announced program objectives are simply descriptions of what the program does. The program will achieve the objective in an almost tautological sense; it is impossible to evaluate the performance of a program even on its own terms. When the announced purpose is "to encourage the production of moderately priced housing" almost any subsidy will fulfill the purpose (unless of course expensive housing is assisted or the program does not influence behavior at the margin). At both the federal and provincial levels there seems to be the assumption that more housing is better than less housing, but there is no explicit recognition of the opportunity costs of the resources used to produce additional housing. Also, there seems to be the assumption that more housing assistance is better than less, but there is no explicit standard of fairness to judge the level of assistance under different programs or the aggregate level of assistance. Existing policy lacks a sufficiently coherent and articulated view of the role of government in housing and mortgage markets to guide the development of specific programs or to assess existing programs.

Instruments of Intervention

In the absence of another standard, this section evaluates current policy using the criteria of welfare economics by comparing the optimal instruments of intervention against the actual instruments.

After analysing the operation of Canadian residential mortgage markets (Fallis, 1983b), it was concluded that the markets basically operate very well. The optimal interventions were confined to documenting cases of unserviced borrowers, making public loans or providing insurance to certain unserviced borrowers and the public provision of mortgage insurance or re-insurance of private mortgage insurance. Mortgage lending might also be used as part of fiscal or monetary policy or as part of a renovation assistance program designed to increase housing consumption.

The federal government has always, under the direct lending program, extended mortgage financing to borrowers who cannot obtain it privately. CMHC offers loans "to applicants who are not able to obtain loans from approved lenders" (CMHC, 1976b). A great deal of such lending occurred in the 1950's and 60's, but it has now almost ceased. CMHC also acts as a lender of last resort under the new non-profit housing program. The provinces have not mounted such programs although much of the lending to rural and native communities, which is coupled with annual assistance, might be construed as lending to unserviced borrowers. However, the direct lending by CMHC is not entirely the same as that envisaged by economic analysis. Those who seek public loans are required to show two rejected loan applications from private lenders and receive credit under "the same terms and conditions and subject to the same limitations as those upon which a loan may be made" under the mortgage insurance or non-profit program (National Housing Act, R.S. 1979). The lending seems designed to give loans to those who satisfy the usual criteria of credit worthiness for NHA loans but who have been denied funds due to some form of credit rationing. The lending is not designed to remedy problems of pooling high risk loans or incorrect information. Nor does CMHC attempt to monitor the problems of unserviced borrowers and analyse whether public lending might improve social welfare. The optimal policy therefore entails somewhat more than present activities.

In providing mortgage insurance, the federal government obviously conforms to the policy recommended by welfare economics. However, the current system of NHA mortgage insurance especially in recent years has gone beyond supplying actuarially sound insurance, to insuring private loans at implicitly subsidized rates. Some have argued that all NHA insurance has been subsidized although this does not show up in the Mortgage

Insurance Fund because of accounting procedures. The fee for originating an insurance application is well below cost, and both fees and operating costs are dealt with in the CMHC operating budget, not the Mortgage Insurance Fund (Task Force, 1979). More significantly, CMHC has insured higher risk private loans made under housing assistance programs such as the Assisted Home Ownership Program and charged only the usual insurance premium. Loans now being insured under the new non-profit program and insured graduated payment mortgages also likely require a higher premium. In order to implement the optimal policy, public mortgage insurance must become actuarially sound, covering all its costs and charging differing premia on the differing risk classes of loans.

Although existing residual lending and mortgage insurance resemble the recommendations of the companion discussion paper, the vast array of federal and provincial assistance programs which involve mortgage lending clearly do not. These programs described in detail in Chapters 2 and 3 were of three sorts: one sort makes mortgage loans to finance the construction of rental accommodation which, coupled with other assistance, permits the units to rent at less than market rates; a second makes mortgage loans to homeowners again usually coupled with assistance to reduce the annual carrying cost of the purchase (often builders use such mortgages to finance new construction and the loan is assumed by the purchaser); and a third sort advances mortgage loans and assistance for renovation of existing housing. In each case, the effect of the program is to reduce the price of housing either to the homeowner or the tenant. Usually, private mortgage financing could have been obtained and the essential public sector role is the provision of continuing assistance.

These programs might be viewed as reactions to the underconsumption of housing, but the optimal interventions to deal with the underconsumption of housing require no such large scale public mortgage lending. Indeed in Canada, it is likely that if the distribution of income were optimal then there would be no problem of the underconsumption of housing.

There are several criticisms of existing programs as responses to the problem of underconsumption of housing. With the exception of public housing tenants, most participants in these programs are lower middle income households and would not underconsume housing in the absence of government help. Certainly, they would consume less housing if they did not participate in the program, but most lived in adequate housing before. This is especially true of rental programs such as the Assisted Rental Program which financed new, good quality apartments with rather low ongoing assistance, and the ownership programs. The eligibility criteria do not include the quality of housing inhabited by an applicant or any proxy for this. Even traditional public housing programs, where many households did underconsume housing before entering, are not the best response to underconsumption problems. Public housing likely raises the level of housing consumption above the threshold where externalities, donor preferences or merit goods operate. Further, the assistance is available only to a small percentage of those households who underconsume housing (Fallis, 1980).[3] Thus, a large subsidy is granted a lucky few and their housing consumption is raised significantly while other similar households receive no assistance.

Within the group of beneficiaries of many housing assistance programs there also is a maldistribution of benefits. A study of federal and Ontario housing programs (Fallis, 1980) found that compared to an alternative equal-cost program[4] under which benefits fell as income rose, most programs were regressive. Lower income participants would gain if a shelter allowance were substituted for existing programs. This maldistribution is compounded when comparisons are made across programs. Many relatively already-well-housed (well-off) households receive more assistance under ownership programs than less well-housed (poorer) households under rental programs. Social welfare would clearly be increased by substituting a price reduction program offering moderate assistance to a larger number of people and with assistance which fell as ability-to-pay increased.

The welfare economic analysis concluded that if housing underconsumption were a problem, it should be dealt with either by shelter allowances or renovation assistance, perhaps with a public mortage loan. The federal and most provincial governments assist renovation, often of both owned and rented premises, providing mortgage loans and subsidizing annual carrying costs. Various forms of shelter allowances also exist which were not described in Chapters 2 and 3 because they did not involve mortgage lending. The federal rent supplements, the British Columbia Shelter Aid for Elderly Renters (SAFER), Ontario's shelter deduction from taxable income, and New Brunswick's Rental Assistance to the Elderly (RATE) program all may be classified as shelter allowances. The federal government does not provide a comprehensive shelter allowance, but has recently debated the possibility of instituting one (CMHC, 1981b). These price reduction programs are the same sort as the recommended optimal interventions. This monograph is not the place to assess whether they are optimally designed.

However, these renovation and shelter allowance programs are only a small part of government intervention. In their totality, existing programs often deliver assistance to the wrong people in the wrong way and the aggregate amount of assistance may be too high. Many of the programs are simply unnecessary.

An alternative view of mortgage lending programs is that they are primarily intended to redistribute income - the aim is to raise the welfare of the recipient rather than to increase their housing consumption. Smith (1977) adopts this view. However, as programs pursuing this objective, the mortgage lending programs to finance the construction of new housing or the renovation of existing housing are also poor policy. A lump sum cash transfer will raise the utility of the recipient more than an equal-cost reduction in the price of housing. Fallis (1980) estimated, for several housing programs, the difference between the actual cost to the government and the cash grant which would leave the recipient just as well off. The largest differences were for homeownership programs and in some instances the difference was 80 per cent of the program cost. For rental programs, the difference was about 35 per cent of program cost. Actual income maintenance systems are not identical to lump sum grants but are likely superior to housing assistance. As an instrument to redistribute income, housing assistance is clearly not optimal and, obviously, mortgage lending programs should not be used to this end.[5]

Viewed as instruments of income redistribution, existing mortgage lending assistance programs also may be criticized for a suboptimal distribution of benefits just as when viewed as instruments to deal with housing underconsumption. Similar households do not receive similar levels of assistance and the level of assistance, within and across programs, does not decline as income rises.

However it is probably more accurate to criticize many mortgage programs as simply unnecessary rather than as maldistributing benefits. This is true whether the programs are considered as attempts to raise housing consumption or redistribute income. Such programs as the Assisted Home Ownership Program at the federal level, or the Home Ownership Made Easy Plan in Ontario, or the Alberta Family Home Purchase Program or Core Housing Incentive Program reduce the price of housing to households who were not underconsuming housing before and are sufficiently well off that they would not be net gainers if the optimal distribution of income were attained. The programs are interventions which were not called for under optimal policy.

The final intervention to consider is mortgage lending to stabilize the economy. Optimal policy could involve direct mortgage lending as a technique of fiscal stimulus and as part of monetary policy, sheltering the housing sector during prolonged and escalating monetary restraint. Interventions to stabilize the housing sector independently of the national economy were not called for.

Evaluation of the actions of government in this regard is rather difficult and certainly cannot rely simply on the statement of program objectives and program descriptions of Chapters 2 and 3. Existing data on housing starts in each year, or the unemployment rate, or gross national product, or the rate of inflation, are data after the interventions of governments. In order to assess the role of public mortgage lending in economic stabilization, a model of the economy is required which would simulate the world in the absence of public mortgage lending and so be able to show the impact of actual public mortgage lending (and its financing) on housing starts and the aggregate level of economic activity. Then it could be established whether actual lending had been stabilizing or destabilizing. Unfortunately, results from macroeconomic models at this level of disaggregation are not available.

Direct examination of the data can however yield some insights. Under the assumption that government policy did not change the direction of fluctuations (for example, did not convert an expansionary period into a contractionary one), observed fluctuations are indicative of the basic pattern of fluctuations which would have occurred without government. Further assuming that public mortgage lending together with its financing does influence aggregate housing starts and aggregate output, and that this influence is without substantial lags, the relationship between public mortgage lending and fluctuations in gross national product and in housing starts may be examined to see whether mortgage lending has tended to stabilize or destabilize fluctuations.

The patterns of fluctuations in housing starts and gross national product expressed as percentage deviation from trend were presented in the companion discussion paper (Fallis, 1983b). These patterns are summarized in Tables 4-1 and 4-2. The changes in federal mortgage lending documented in Tables 2-1, 2-2 and 2-3 of Chapter 2 are examined for each period of the fluctuations in GNP or housing starts and judged to be either re-enforcing or dampening. These data must be interpreted cautiously for they are annual data concealing significant variation within a year and the conclusions will be somewhat sensitive to the dating of the fluctuations (although government lending has been assumed to be such that the actual and hypothesized-without-government cycles are in phase, the turning points of each are not likely the same). Furthermore, the approach does not reveal whether mortgage lending was deliberately used as an instrument of stabilization or was coincidentally dampening fluctuations.

Nevertheless, it may be reasonably concluded that lending has been used as an instrument to stabilize housing construction.[6] This conclusion is re-enforced by examining the timing of major changes in lending policy and CMHC's announced explanations of these as intended to stimulate housing starts. Smith (1974) examined the residual lending program alone (the program most suitable as an explicit stabilization instrument) rather than all mortgage lending and reached a similar conclusion. Large increases in direct lending occurred in late 1957, late 1960, late 1966, and late 1970, all of which were troughs in housing starts; and large contractions occurred in mid 1958, early 1960, mid 1961 and late 1967, three of which were in expansionary phases (Smith, 1974, 151).

In six of the eleven periods in Table 4-2, mortgage lending dampened fluctuations in housing starts. During several of the other periods, lending began with a dampening influence, usually increasing when housing starts were in a trough but continued to grow albeit more slowly and so was judged to re-enforce the expansion at the peak. The 1974-1976 period is a good example. Thus although the instrument has been used, it is unclear whether on balance it has reduced or increased housing construction fluctuations. Certainly several troughs were not as deep as they otherwise would have been, but several peaks were also higher as a result. The welfare economic analysis rejected a housing stabilization policy because it was unlikely to be successful enough to yield any reduction in the long run average cost of housing. The actual performance of government gives some support to this conclusion.[7]

The optimal instruments for stabilizing the national economy did include using mortgage lending for fiscal stimulus. Table 4-1 reveals lending has tended to reduce fluctuations in the national economy both during periods of expansion and contraction. It is probable however this stabilizing influence was inadvertent. The purpose of changing levels of lending was not to stabilize the national economy, rather as indicated above, it was to stabilize the fluctuations in housing construction. Since 1967 the national economy and the housing sector have fluctuated together and so a policy addressed to one has beneficially affected the other. Only in the early 1980's has mortgage lending policy been clearly intended to be part of overall macroeconomic policy. The recent Canada Rental Supply Plan, Canada Home Renovation Plan, and Canadian Homeownership Stimulation Plan can be regarded as attempts to stimulate the housing sector in the context of a tight monetary policy (rather than programs dealing specifically with housing issues).

Macroeconomic policy therefore, while recognizing mortgage lending as an instrument, has not used it explicitly, except recently as part of fiscal and monetary restraint. A full assessment of the use of mortgage lending for stabilization would require that the optimal macroeconomic policy of the last few decades be identified, and the role of mortgage lending separated and compared with actual mortgage lending - an impossible task given the current state of economic science. However it can certainly be concluded that mortgage lending has not been overused as an instrument of stabilization.

Costs of Non-Optimality

In welfare economics, the purpose of government intervention in the economy is to maximize social welfare. Any deviation from the optimal policy - more intervention than was called for, using the wrong instrument or wrong design of the instrument, or not intervening where required - will reduce social welfare below what could be attained. The cost of non-optimality is therefore this foregone social welfare.

The previous section of this chapter compared the optimal instruments with the mortgage lending programs of the federal and provincial governments. The largest differences were in the area of housing assistance programs, while in others the differences were relatively small. The existing residual lending likely left some borrowers unserviced and made some loans on more attractive terms than was optimal. Mortgage insurance did secure competitive behavior in the industry for most classes of mortgage loans but also subsidized the insurance on some loans permitting mortgages to be advanced which would not have been in the optimal world. The attempts to stabilize residential construction had unclear results and likely did not reduce (or increase) long-run average housing costs. Housing assistance programs, however, were of the wrong sort and often went to the wrong people. It is here that the social welfare losses are greatest.

Although perhaps obvious, it should be noted that this approach compares the existing world with that which would exist with optimal policy. It does not compare the existing world with what it would have been in the absence of existing programs. The establishment of some programs raised social welfare and therefore to cancel them would reduce welfare. For example, public housing for elderly poor households financed by an increase in the personal income tax likely raises social welfare. However, there are costs to program in the sense that social welfare would be higher still if the equivalent assistance were provided through income supplements.

The reduction in social welfare resulting from all the non-optimal mortgage market activities can be caused in a number of different ways. For example, the stock of housing might be too large. Too many resources are devoted to the production of housing and social welfare would be raised by shifting resources into other uses - perhaps hospitals, or job training programs or natural gas pipelines. Or assistance might be delivered to households who are not underconsuming housing. Social welfare could be raised by shifting the assistance to a household which is underconsuming housing services. Rather than discussing each housing program, the various types of reduction in social welfare will be discussed considering all federal and provincial mortgage lending collectively. Implicitly at least, these costs have already been identified in the comparison of actual and optimal policy.

The mortgage lending and mortgage insurance activities of government have no doubt significantly increased the total stock of housing in Canada. Not all government mortgage loans, of course, finance a net addition to the stock because some of this credit could have been obtained privately and the financing of the program likely raises interest rates and reduces private construction. The issue is whether the housing stock is larger than the optimal stock and thus resources would yield greater social welfare in other uses. The deviations from optimal policy in dealing with unserviced borrowers, mortgage insurance and stabilization discussed in the previous section do not significantly increase the housing stock. The housing assistance lending is more clearly sub-optimal but it is unclear whether the existing stock is too large. Optimal policy would redistribute income through income supplements, perhaps with some small housing assistance programs. Both procedures would significantly increase the housing demand of the recipients. The substitution of an optimal policy for current mortgage lending is unlikely to call for a smaller housing stock.

Recently, Smith (1981) and Downs (1980) have suggested that the stock of housing may be too large in Canada and the United States, respectively. Their admittedly tentative conclusions are based on evidence of the high quality of the housing enjoyed by households, the obvious need for huge investment in energy production and in the modernization of industrial plant and evidence of declining productivity. Even if their conclusions were correct, the extra housing stock is not primarily attributable to mortgage market interventions. As both authors point out, the largest subsidies to housing are tax expenditures under the personal income tax system. Smith estimates that about 80 per cent of federal housing assistance is through tax expenditures.

Social welfare can also be reduced if programs are inefficient in design, in the sense that a certain result could have been achieved using fewer resources. Considering simply the costs of administering mortgage lending and insurance activities, the efficiency costs are unlikely very large. Some would argue that the civil service is inefficient because the system contains few incentives for cost saving, but there has been no careful empirical analysis to accept or reject the claim. The resource costs of administering unnecessary programs or those delivering assistance to the wrong households are a loss, although in the optimal world there would be a more extensive income maintenance system requiring resources for administration.

A more significant inefficiency arises if mortgage loans are used as part of a price reduction strategy to redistribute income to the poor,[8] for example the public housing program. The same increase in utility could have been achieved at less cost to the government, in some cases as much as 80 per cent less. Potential savings are in the tens of millions of dollars.

Finally, the maldistribution of assistance is also a cause of reduced social welfare. To substitute income support for current programs assisting the poor and to cancel the mortgage lending which assists middle income households (with a parallel reduction in taxes or borrowing) would reduce the welfare of some households and raise the welfare of others. On balance, social welfare would be increased. To quantify the potential gains would require that the social welfare function and household utility functions be specified. It is clear however that the gains are large and offer a real opportunity for increasing social welfare.

Thus the evaluation of existing mortgage market interventions in this chapter reveals a mixed picture when comparing them with the recommendations of welfare economics. In dealing with unserviced borrowers and mortgage insurance, current policy coincides roughly with optimal policy and the deviations do not impose significant costs. There has been too much effort devoted to trying to stabilize fluctuations in housing construction, but other than the costs of program administration, social welfare has been little effected. It is on attempts to deal with housing underconsumption and income distribution that criticism must be focussed. Mortgage lending and housing assistance are inappropriate instruments. Much of the assistance flows to households who neither underconsume housing nor require income transfers. It is there that a change in policy would yield the greatest increase in social welfare.

Table 4-1

Federal Mortgage Lending and the National Economy

Fluctuations in GNP			Federal Mortgage Lending	
Trough	Date of Peak	Trough	(+re-enforcing)[1]	(-dampening)[2]
	1952	54		n.a.
54	56	61	-	-
61	66	67	+	-
67	69	70	-	-
70	73	80	-	+

[1] Lending was judged to be re-enforcing if it rose during a trough-to-peak period or if it fell during a peak-to-trough period.

[2] Lending was judged to be dampening if it fell during a trough-to-peak period or if it rose during a peak-to-trough period.

Table 4-2

Federal Mortgage Lending and Housing Starts

Fluctuations in Housing Starts			Federal Mortgage Lending (+re-enforcing)[1]	(-dampening)[2]
Trough	Date of Peak	Trough		
51	55	57		-
57	58	60	+	+
60	64	66	+	-
66	69	70	-	-
70	73	74	-	-
74	76	80	+	+

1,2 See notes in Table 4-1.

Chapter 4: Notes

1 Programs to assist those who must refinance their homes at much increased interest rates and may have to sell their houses are best considered as part of stabilization policy. If stabilization policy forces a household to sell their house, this might be considered a hardship which should be cushioned in the same way as unemployment.

2 An alternative approach is to assume government follows welfare economics and to categorize existing programs according to which rationale for government intervention they seem consistent. Smith (1978) provides such a categorization.

3 This is partly because these programs are very costly per household participating (the programs raise housing consumption significantly).

4 Under the alternative program, the percentage fall in benefits was equal to the percentage rise in income across income classes.

5 Even if housing assistance were the optimal policy, public mortgage lending might not be the optimal instrument. The essential aspect of the assistance is not lending but the subsidy of annual costs.

6 Certain lending programs such as the Assisted Rental Program have been used to stimulate certain sorts of new construction. Here the concern is with all mortgage lending.

7 A similar analysis of provincial mortgage lending or the aggregate of federal and provincial lending could not be undertaken because there is no consistent time series of provincial mortgage lending.

8 This of course does not include all of the housing assistance programs. Many deliver assistance to middle income households and seem justified neither on the basis of housing underconsumption or income redistribution.

5 SUMMARY AND CONCLUSIONS

The analysis of this and the companion discussion paper (Fallis, 1983b) has been devoted to examining government involvement in residential mortgage markets. It began by developing the recommendations of economic theory for the optimal intervention in mortgage markets. Then the existing mortgage programs of the provincial and federal governments were described. Together these two parts permitted an evaluation of current policy. This short chapter provides a summary of the analysis and main conclusions.

Welfare economics measures the performance of an economy using a social welfare function in which the level of social welfare depends on the utility of households which in turn depends on the consumption of households.1 Theory asserts that an economy without government will achieve the maximum social welfare if markets are competitive; there is no uncertainty; there are no technological externalities; there are no merit goods; the distribution of income is fair and there are no stabilization problems. If the stringent conditions of this list all hold, there is no need for government intervention. If any condition is not fulfilled, the possibility exists that government intervention might improve social welfare. The items on the list therefore define the possible roles for government. By examining each in the context of housing and mortgage markets, the possible roles in mortgage markets can be identified. The optimal instrument of intervention will be that which maximizes social welfare.

To establish whether lack of competition is a problem requiring a mortgage market intervention, several markets were examined. These included not only the mortgage lending and mortgage insurance markets, but also the output markets for new, used, owned and rented housing and other input markets for land, labour and materials. It proved to be only the mortgage insurance market where intervention was suggested. The optimal response was to continue publicly providing mortgage insurance or to institute public re-insurance of private mortgage insurance. The administration of the mortgage insurance program by CMHC should however be altered to ensure that the premia are sufficient to cover all costs of operation as well as provide adequate reserves against claims and that the premia differentiate among risk classes of loans.

The Canadian economy, like all economies, is obviously characterised by uncertainty but it is much less obvious what government can do to improve social welfare. Information is a commodity which is costly for either governments or the private sector to produce. There exists the possibility that private financial institutions underinvest in high risk mortgage loans or have incorrect information about the credit worthiness of some households. However, the case has not yet been proven. The government ought to analyse the problems of unserved borrowers, being prepared to offer redress via insurance or public mortgages with appropriate risk premia, rather than immediately embark on a public lending program. Residual lending by CMHC is currently very small and takes a much narrower approach, confining itself to those who meet NHA qualifications but have been refused credit.

It was concluded that Canadian mortgage markets operate quite well. The existing policies are limited to public mortgage insurance and some residual lending and reflect that Canadian governments have reached a similar conclusion. Existing and optimal policies do not diverge significantly and such differences as exist do not cause major reductions in social welfare. However, most mortgage lending of federal and provincial governments has not been designed to remedy capital market failures but rather has been part of housing programs designed to raise housing consumption and to redistribute income.

Welfare economics offers several reasons why private decisionmakers might consume less housing than they would at the social welfare maximum. There may be positive externalities from housing consumption; there may be interdependence among people in which the consumption of housing by individual A is an argument in the utility function of individual B; or housing may be a merit good such that the housing consumption of each household is an argument in the social welfare function. In each case, the private decisionmaker, thinking only of his own gain in utility from increased housing consumption, does not consider the other positive effects on social welfare and so may underconsume housing services. The positive effects likely cease when housing consumption rises above a certain threshold.[2] The optimal policy to deal with underconsumption is to reduce the price of housing to those consuming below the threshold. The price reduction should be achieved through a shelter allowance or in some cases a combination of shelter allowance and assistance for housing renovation perhaps secured by public mortgage loans.

Most government mortgage loans whether provincial or federal are provided as part of a program which reduces the price of housing services to the participants. Some loans finance new construction of houses to be later assumed when a household buys the home, others finance new construction of rental housing and still others finance the purchase of existing housing. The federal government and every province has at some time made these sorts of loans. Some governments also finance renovation of owned and rented housing but this is a very small part of total lending activitiy.

Judged as attempts to deal with the problem of housing underconsumption, these programs are inappropriate. Many of the beneficiaries did not underconsume housing before and thus reducing the price of housing to them is simply unnecessary. Even when households did underconsume housing, the response is badly designed because the price reduction is so significant that housing consumption rises far above the threshold where external effects on social welfare operate.

Alternatively, the lending could be judged as an instrument of income redistribution which is another rationale of welfare economics for government intervention. Most would agree that the distribution of income at the social welfare maximum in Canada would be more equal than the distribution of a laissez-faire economy and therefore purchasing power should be redistributed. However, in pursuit of this goal, existing mortgage lending programs are also inappropriate. Many of the beneficiaries of housing programs would be net contributors to an optimal system of redistribution and should not receive a reduced price of housing. Equally important, social welfare is higher when income is redistributed through cash payments rather than price reductions and so optimal policy would not involve mortgage lending.

Some households in Canada underconsume housing and would be the recipient of net transfers at the social welfare maximum. Two rationales for intervention exist simultaneously. However, if the distribution of income were optimal, the cases of housing underconsumption would likely be very few and thus the focus of public policy should be on income distribution.

The final item on the list of possible government interventions is the stabilization of economic fluctuations. A public mortgage lending program might be the optimal instrument of fiscal stimulus if the housing industry had substantial idle resources at the time stimulus was required. Or it might be part of an optimal restrictive monetary policy reducing the disproportionate impact of prolonged high interest rates on housing construction. It is not necessarily a part of every expansionary fiscal policy or contractionary monetary policy, but should be retained as a possible instrument. The federal government has seldom used mortgage lending as part of stabilization policy although in the last fifteen years changes in mortgage lending have tended to dampen slightly fluctuations in the national economy. This is because housing construction and the national economy have tended to fluctuate together and mortgage lending has been used to stabilize housing construction. However, any success in stabilizing housing construction has been modest and certainly insufficient to reduce long-run housing costs.

The consideration of each rationale for intervention thus reveals that the optimal interventions in mortgage markets are neither numerous nor large. Aside from the provision of mortgage insurance, what is required is analysis and monitoring with an ability to make public mortgage loans to deal with specific unserviced borrowers, or certain cases of housing underconsumption or to stabilize the economy where conditions warrant. Mortgage lending ought to remain an instrument of public policy. But there is no need to use it to increase the total stock of housing or to redistribute income or to raise levels of housing consumption. Hundreds of millions of dollars in mortgage loans have been made each year by the federal government and the provinces loan equally large amounts. Social welfare could be raised significantly by reducing these lending levels.

Chapter 5: Notes

1 With merit goods, both consumption and utility levels can be arguments of the social welfare function.

2 The threshold may be different depending on whether externalities, donor preferences or merit goods are at issue, but in each case a threshold surely exists.

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POOR

QUALITY

ORIGINAL